
SELF ASSESSMENT

ON OBSERVANCE BY NASDAQ CSD SE

OF THE CPSS-IOSCO PRINCIPLES FOR FINANCIAL MARKET

INFRASTRUCTURES

04.10.2016

Responding institutions:

Eesti Väärtpaberikeskus AS (“**CSD EE**”), registration no. 10111982 with the Estonian Trade Register,

AB "Lietuvos centrinis vertybinių popierių depozitoriumas" (“**CSD LT**”), registration no. 110059343 with the Lithuanian Register of Legal Entities,

AS “Latvijas Centrālais depozitārijs” (“**CSD LV**”), registration no. 40003242879 with the Commercial Register of Latvia,

which after the merger of CSD EE and CSD LT into CSD LV will assume the rights and obligations of CSD EE and CSD LT and will act as a surviving company under the name of Nasdaq CSD SE (“**Depository**”), but CSD EE and CSD LT as merged companies will cease to exist without liquidation.

Jurisdiction(s) in which the FMI operates: Estonia, Latvia and Lithuania

Authority(ies) regulating, supervising or overseeing the FMI:

(A) Supervision of the Depository:

Financial Capital Market Commission (“**FCMC**”) acting as home Member State supervisor under the CSDR, <http://www.fktk.lv/en/>

Estonian Financial Supervision Authority acting as host Member State supervisor under the CSDR, <https://www.fi.ee/>

Bank of Lithuania acting as host Member State supervisor under the CSDR, <https://www.lb.lt/>

(B) Oversight:

Estonian securities settlement system – Bank of Estonia (*Eesti Pank*), <http://www.eestipank.ee/en>

Latvian securities settlement system – Bank of Latvia (*Latvijas Banka*), <https://www.bank.lv/en/>

Lithuanian securities settlement system – Bank of Lithuania (*Lietuvos Bankas*), <https://www.lb.lt/>

The date of this disclosure is: 04.10.2016

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Abbreviations	Explanation
A2A	Application-to-Application
Baltic CSDs	Eesti Väärtpaberikeskus, AS “Latvijas Centrālais depozitārijs” and AB "Lietuvos centrinis vertybinių popierių depozitoriumas"
CeBM	Central Bank Money
CoBM	Commercial Bank Money
CSA	Technical cash settlement account in CSD System. ¹
CSD EE	Eesti Väärtpaberikeskus AS
CSD LT	AB "Lietuvos centrinis vertybinių popierių depozitoriumas"
CSD LV	AS “Latvijas Centrālais depozitārijs”
CSD System	A set of hardware, software and other technical infrastructure components through which the Depository provides securities clearing, settlement and other services
CSDR	Regulation (EU) No 909/2014 on securities settlement and on central securities depositories
DCA	Dedicated Cash Account
DCP	Directly Connected Party
DvP	Delivery versus payment
ECB	European Central Bank
ECRS Act	Estonian Central Register of Securities Act
GUI	Graphical User Interface
FoP	Free of payment
FSA	Financial services authority
ICP	Indirectly Connected Party
ISD	Intended Settlement Date
ISIN	International securities identification number
NCB	National Central Bank
OTC	Over the counter
RTGS	Real-time gross settlement
RTS	CSDR Regulatory Technical Standards
Rules or Rulebook	Rules of Nasdaq CSD SE.
SED LT	Lithuanian Law on Settlement Finality in Payment and Securities Settlement

¹ CSD System refers to CSD software DEPEND that is used for operation of Settlement Systems of the Depository, including for the record keeping, data processing and information exchange that is necessary to comply with T2S FWA, maintaining Estonian Register of Securities and providing other CSD services. Functionality of CSD System is available to Participants through special-purpose client application (GUI of CSD System) and other communication channels provided in operating manual(s) and technical documentation of Nasdaq CSD SE.

	Systems
SFD LV	Latvian Law on Settlement Finality in Payment and Financial Instrument Settlement Systems
SMA	Estonian Securities Market Act
TARGET 2 (T2)	The entirety resulting from all TARGET2 component systems of the NCBs. TARGET2 component system is any of the NCB's real-time gross settlement (RTGS) systems that form part of TARGET2
T2S	Pan-European platform for securities settlement operated by Eurosystem

I. Executive summary

This self-assessment is prepared in the contemplation of the merger of CSD EE and CSD LT into CSD LV. As a result of the merger, CSD LV will assume the rights and obligations of CSD EE and CSD LT and will continue to act as a surviving company under the name of Nasdaq CSD SE (hereinafter the merged company is referred to as the "**Depository**"), and CSD EE and CSD LT as merged companies will cease to exist without liquidation. This self-assessment disclosure relates to the Depository acting as:

- (i) a central securities depository ("**CSD**") authorised by the FCMC to provide CSD services under the Central Securities Depositories Regulation² ("**CSDR**") in Latvia, in Estonia and Lithuania via its Estonian and Lithuanian branch, respectively, and acting as the registrar of the Estonian Register of Securities via its Estonian branch;
- (ii) the operator of **Estonian Settlement System** designated as a securities settlement system governed by Estonian law and notified to the European Securities and Markets Authority ("**ESMA**") in accordance with the Settlement Finality Directive;³
- (iii) the operator of **Latvian Settlement System** designated as a securities settlement system governed by Latvian law and notified to the ESMA in accordance with the Settlement Finality Directive; and
- (iv) the operator **Lithuanian Settlement System** designated as a securities settlement system governed by Lithuanian law and notified to the ESMA in accordance with the Settlement Finality Directive (each settlement system under (ii) to (iv) individually referred to as "**Settlement System**").

This self-assessment is provided considering that:

- (i) The appropriate amendments in the local laws that are applicable to the Depository and Settlement Systems operated by the Depository will be made;
- (ii) At the time when the authorization to the Depository under CSDR will be granted, it is going to provide settlements only in euros;
- (iii) At the time when the authorization to the Depository will be granted the following link arrangements will be effective:
 - Clearstream Banking Luxembourg S.A ("**Clearstream LUX**" or "CBL") which enables the Participants to hold and settle transactions with securities registered with Clearstream LUX as Issuer CSD; and
 - Krajowy Depozyt Papierów Wartościowych S.A. ("**Polish CSD**" or "KDPW") which enables the Participants of Polish CSD to hold and settle transactions on FoP basis with securities registered with the Depository as Issuer CSD.

The Depository will operate reliable, effective, low risk and efficient securities Settlement Systems. The Depository has clear and transparent rules and procedures in place to run its operations and allow its participants to deal with the risks they face in operating and using any Settlement System. The Depository's rules and procedures comply with the requirements of the CSDR and applicable law.

The Supervisory Council and the Management Board of the Depository are strongly committed to maintain a very low risk profile of the Depository by limiting its activities to core CSD services and

² Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012.

³ Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality (with amendments).

certain non-banking type ancillary services that do not entail credit and liquidity risks. This commitment is reflected in conservative and well-designed operational model of the Depository.

This document represents the Depository's first disclosure that is made in accordance with "*CPSS-IOSCO Principles for financial market infrastructures of April 2012*" and disclosure framework thereof. The answers to the questions are structured as follows:

- (i) first, description applicable to all the Settlement Systems operated by the Depository or the Depository as a whole is provided;
- (ii) second, country specific differences applicable to a particular Settlement System operated by the Depository or participants to such Settlement System (if any) are provided;
- (iii) in case the answer does not expressly distinguish between different Settlement Systems, the answer applies to all the Settlement Systems or the Depository as a whole.

The capitalised terms used in the answers have the meaning provided in the Rules, unless expressly stated otherwise.

CSD EE, CSD LV and CSD LT (which will be replaced by the Depository) have concluded that the Depository broadly observes every principle relevant to the CSDs and SSS.

Minor reservation applies for principle 15 with respect to recovery and orderly wind-down plan: this is work in progress to be finalised immediately following the publication (in the Official Journal) of the RTS on prudential requirements of CSDs.

The Depository has not assessed itself against Principles 6 and 14 as they are not applicable to CSDs and operators of securities settlement systems.

The Principle 5 is not applicable to the Depository since the Depository does not operate collateral management system itself, does not provide credit to its participants and is not involved in management of participants' collateral exposures. The Depository provides only collateral settlement services for its participants' bilateral operations.

The Depository has not assessed itself against principle 10 since the Depository does not provide services related to delivery of physical instruments and commodities.

The Depository intends to disclose majority of its detailed responses provided in the course of oversight assessment.

II. General background on the FMI

General description of the FMI and the markets it serves

Formation of the Depository via cross-border merger of the Baltic CSDs

The Depository will be formed by September 2017 *via* a cross-border merger of the three existing Baltic central securities depositories as the result of which:

- (i) CSD LV will continue operating as a surviving company by changing its legal form to *Societas Europaea* (SE) and the name to “Nasdaq CSD SE”;
- (ii) CSD EE as a merged company will cease to exist without liquidation and the Depository (through its Estonian branch) will assume all the rights and obligations of CSD EE other than pension register services which might be provided by Estonian subsidiary of the Depository;
- (iii) CSD LT as a merged company will cease to exist without liquidation and the Depository (through its Lithuanian branch) will assume all the rights and obligations of CSD LT.

The cross-border merger of the three Baltic CSDs involves the following milestones:

- (i) CSD LV, CSD EE and CSD LT will conclude a merger agreement on the first half of 2017;
- (ii) CSD LV will establish dormant branches in Estonia and Lithuania;
- (iii) CSD LT and CSD EE will be merged into CSD LV via an upstream merger, and CSD LV will assume the rights and obligations of CSD EE (through its Estonian branch) and CSD LT (through its Lithuanian branch);
- (iv) CSD LV will complete the cross-border merger by registering the merger and transformation of its legal form in SE with the Latvian Commercial Register and CSD EE and CSD LT will be deleted from the respective public registers in Estonia and Lithuania.

In parallel to the cross-border merger process, CSD LV intends to obtain an authorisation under the CSDR to provide core CSD services and certain non-banking type ancillary services in Latvia and to passport such authorisation to Estonia and Lithuania on the basis of freedom of establishment (i.e. via a branch). Subject to compliance with the regulatory and technical requirements and authorisations, it is planned that in September 2017 the Depository will:

- (i) commence providing CSD services in Latvia, Estonia and Lithuania as a CSD authorised under the CSDR and will act as an operator of the Estonian Settlement System, the Latvian Settlement System and the Lithuanian Settlement System;
- (ii) switch from the existing technical platforms of the three Baltic CSDs to one common CSD System; and
- (iii) migrate all the securities account balances held with all the Settlement Systems to T2S Platform (except where the Rulebook expressly provides otherwise).

Organisation, supervisory and oversight framework of the FMI

The Depository, with its head office in Latvia and branches in Estonia and Lithuania, will be authorised by the FCMC to provide CSD services under the CSDR and to act as the registrar of the Estonian Register of Securities. The Depository operates in the form of *Societas Europaea* (SE) within the meaning of the Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE), in accordance with Latvian Commercial Law and the Law on European Companies.

The Depository is part of the Nasdaq Group, with Nasdaq Inc. (organisation No. 52-1165937) as the ultimate parent, which is providing trade and post trade services in more than 50 countries.

Due to market situation in settlement, notary and central maintenance services the Settlement Systems operated by the Depository are of a systematic importance for the functioning of securities markets in Estonia, Latvia and Lithuania.

The Depository is supervised by:

- (i) FCMC acts as a home Member State supervisor under the CSDR.
- (ii) Estonian Financial Supervision Authority acts as a host Member State supervisor under the CSDR; and
- (iii) Bank of Lithuania acts as a host Member State supervisor under the CSDR.

The Settlement Systems operated by the Depository are subject to the oversight of the respective national central bank:

- (i) Estonian Settlement System is subject to oversight of the Bank of Estonia;
- (ii) Latvian Settlement System is subject to oversight of the Bank of Latvia
- (iii) Lithuanian Settlement System is subject to oversight of the Bank of Lithuania.

Supervisors and overseers intend to sign Cooperation Agreement on the cooperation framework for the supervision and oversight of the Depository.

Management and governance

The Depository is a private sector company, that is 100% owned subsidiary of Nasdaq Nordic Ltd.. Nasdaq Nordic Ltd is owned through a chain of holding companies by Nasdaq Inc., a company incorporated in Delaware, USA.

The Depository's governance legal framework consists of statutory provisions (Latvian Commercial Law, the CSDR and the Law on Financial Instruments Market of Latvia), as well as Articles of Association and internal policies and procedures.

In accordance with the CSDR, and the Latvian Financial Instruments Market Law and the articles of association, the Depository is going to be run by the following bodies:

- (i) **Supervisory Council** - responsible for planning the activities of the company, organising the management of company and supervising the activities of the Management Board as well as will be responsible for fulfilment of the obligations imposed by the CSDR to the management body ;
- (ii) **Management Board** - responsible for day-to-day management of the company, including that the operations and accounting of the Depository are adequately organised as well as will be responsible for the fulfilment of the obligations imposed by the CSDR to senior management.

In accordance with the CSDR the Depository is going to established also the following committees:

- (a) **User Committee of each Settlement System** that is going to exercise oversight, in an advisory role, over the activities of the Depository which the User Committee considers to be key issues that impact the issuers and participants of the respective Settlement System. The User Committee advises the Supervisory Council on key arrangements that have impact on participants of the Settlement System, the criteria for admission of

securities or participants to the Settlement System, the service level of Depository and other matters which may have impact on participants of the Settlement System.

- (b) **Risk committee** that is going to be responsible for advising the Supervisory Council on the Depository's overall current and future risk tolerance and strategy. The risk committee is going to be chaired by a person with appropriate risk management experience and who is independent from the Depository's executive members of the Supervisory Council.
- (c) **Audit committee** that is going to be responsible for advising the Supervisory Council on the performance of the Depository's independent internal audit function, which it shall oversee. The audit committee is going to be chaired by a person with appropriate audit experience and who is independent from the Depository's executive members of the Supervisory Council.
- (d) **Remuneration committee** that is going to be responsible for advising the Supervisory Council on the Depository's remuneration policy, which it shall oversee. The remuneration committee is going to be chaired by a person with appropriate experience and who is independent from the Depository's executive members of the Supervisory Council.

The Depository has robust governance arrangements, which include a clear organisational structure with well-defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks to which it is or might be exposed and internal control mechanisms in compliance with CSDR. Please see Annex 1 for more details about future organisational chart of the Depository.

The Depository is the part of Nasdaq group. The primary responsibility for managing risks is aligned with the line management structure within Nasdaq group. Managers at all levels are responsible for the efficient implementation and execution of risk management within their own area of operational responsibility.

In legal terms, the Nasdaq Inc. Board of Directors has the overall responsibility for ensuring that an adequate and well-functioning process for risk management has been implemented throughout the group. The management (including Management Board and Supervisory Council or other similar collective bodies of management) of each legal entity have the fiduciary risk management duties relating to the respective legal entity. This also includes managing specific risk related issues as governed by local regulatory requirements or local market practices. To support management bodies, a role of Risk Coordinator has been designed for each regulated legal entity within Nasdaq group. The Risk Coordinator of the Depository shall also fulfil the role of chief risk officer within the meaning of CSDR. Risk Coordinator has a direct reporting line to Management Board of the Depository and direct access to the Supervisory Council of the Depository.

The main duties of the Risk Coordinator in relation to the Depository are:

- (i) to provide assurance to the management bodies that the Depository is compliant with legal and regulatory requirements in the area of risk management.
- (ii) to provide support to the management in related regulatory issues.
- (iii) to facilitate any coordination efforts that may be required for the legal entity to exercise control over its own risk environment.
- (iv) to provide assurance that appropriate plans and procedures, specific to the legal entity, has been developed and are properly maintained and tested.

- (v) maintain documentation, specific to the legal entity, in an assigned repository shared with other members within the network of Risk Officers and Coordinators of Nasdaq Group.
- (vi) liaise with Risk Officers within the business line organization, to ensure that the legal perspective is being addressed and that the legal entity is able to operate accordingly.

Global Risk Management is responsible for providing information, training, support and guidance to the Risk Coordinators in fulfilling their roles.

Responsibilities of statutory managing bodies are documented in the Depository's articles of association and the relevant rules of procedure.

All below mentioned key elements regarding the Depository's governance will be publicly disclosed at official website of the Depository:

- (i) Description of the Nasdaq Nordic Ltd. and its ownership in Baltic financial market infrastructure entities;
- (ii) Depository's articles of association;
- (iii) composition of the Depository's management bodies.

CSD services

Please refer to <https://nasdaqcsd.com/> (Service Description of the Depository) for descriptive overview of CSD services of the Depository following its migration to T2S.

The Depository provides all three core CSD services: initial recording of securities ("**notary service**"), maintaining of securities accounts at the top tier level ("**central maintenance service**") and settlement services ("**settlement services**").

In addition, the Depository is going to provide certain non-banking-type ancillary services of CSDs, as it will be specified in its authorization, and the following country-specific services:

- (i) In Latvia, the Depository keeps initial register of shareholders for privatized companies until the owners of securities have opened a securities account with a System Participant to the Latvian Settlement System and provides savings notes registry services.
- (ii) In Lithuania, the Depository provides savings notes registry services.

Participation

An entity holding or seeking the status of the Depository's Participant can apply for the system participant status ("**System Participant**") in one or more Settlement Systems with one or more of the following statuses:

- (i) an Account Operator;
- (ii) a Cash Agent;
- (iii) an Issuer Agent;
- (iv) a Fund Administrator; and
- (v) a Foreign CSD as Investor CSD.

The System Participant to several Settlement Systems has access to securities recorded in such systems by means of harmonised set of procedures of the Depository and integrated C SD System.

Notary services

The Depository is going to provide notary services through its head office in Latvia and branches in Estonia and Lithuania. The Depository provides notary services provided that securities for which admission is requested comply with the admission criteria and other provisions of the Rules. In the capacity of a member of Association of National Numbering Agencies (**ANNA**), the Depository assigns ISIN and classification of financial instrument (**CFI**) codes to the securities initially registered with any Settlement System through its head office in Latvia and branches in Estonia and Lithuania.

As a general rule, the Depository admits securities to the “home” Settlement System for the respective Issuer:

- (i) shares of companies registered in Estonia and other securities constituted under Estonian law are admitted to Estonian Settlement System;
- (ii) shares of companies registered in Latvia and other securities constituted under Latvian law are admitted to Latvian Settlement System;
- (iii) shares of companies registered in Lithuania and other securities constituted under Lithuanian law are admitted to Lithuanian Settlement System.

Notwithstanding the above, the Depository may admit securities of a foreign Issuer (i.e. issuer that is incorporated in the different jurisdiction from the jurisdiction of Settlement Systems where initial recording of securities is applied for) wishing to exercise the freedom of issue to any Settlement System provided that the Issuer complies with the admission requirements and the Depository complies with Articles 23(3) (e) and 49 of the CSDR.

Central maintenance services

The System Participant or the investor acting through the System Participant may open in its name various **types of Operational Accounts** that are used only for aggregate accounting of securities in those Settlement Systems where the Participant has acquired the status of the System Participant. **Securities account** for the securities of the same ISIN is created upon the first credit of the respective securities for the benefit of the holder of Operational Account.

The Depository offers the account types that enable to hold with any Settlement System nominee accounts in the name of the System Participant or the client of the System Participant and owner accounts in the name of the end investor.

Each securities account has a **unique account number** composed of:

- (i) the number of the Operational Account which allows to determine the type of such account and legal implications of holding securities in such account (e.g. level of asset segregation and entitlement to securities, where applicable); and
- (ii) ISIN of the securities credited for the benefit of the holder of Operational Account which allows determining the Settlement System in which the securities are initially recorded and, hence, determine the law applicable to securities holding.

Securities which are registered with the Depository as Issuer CSD are held with the Settlement System in which the securities are registered. Securities which are held with the Depository as Investor CSD through CSD link arrangement with a foreign CSD are deemed to be held in the default Settlement System of the Account Operator, unless the Account Operator has selected a different default Settlement System for the specific operational account. Thus, proprietary aspects (entitlement to securities, pledge rights and other rights *in rem*) of securities held by the account holder with:

- (i) Estonian Settlement System are governed by Estonian law;
- (ii) Latvian Settlement System are governed by Latvian law;
- (iii) Lithuanian Settlement System are governed by Lithuanian law.

Settlement services

The Depository executes the settlement instructions of the account holders only if the Account Operators have fulfilled all the requirements set out in the Rulebook and Operating Manual.

The Depository through its Settlement Systems, among others, provides the following services:

- (i) settlement of stock exchange trades;
- (ii) matching of OTC transactions;
- (iii) settlement of free-of-payment (OTC FoP) transactions;
- (iv) settlement of delivery versus payment (OTC DvP) transactions;
- (v) settlement of cross-border stock exchange and OTC transactions under CSD link arrangements.

The Depository intends to provide settlement of cash leg in respect of DvP transfer orders and distribution of corporate action proceeds only in euro currency in CeBM. The cash leg for DvP transfer orders in T2S eligible securities is settled via DCAs of Payment Banks in T2S and for DvP transfer orders in non T2S eligible securities via cash account in T2 Component System. In the future, the Depository may designate a special purpose credit institution for the settlement of cash leg in other currency than euro, subject to availability of such credit institution operating in the Baltic market and compliance with the CSDR.

The Depository does not maintain settlement links between the Settlement Systems operated by the Depository. The securities initially recorded in one Settlement System of the Depository, or transferred to such Settlement System from a foreign CSD as Issuer CSD, cannot be transferred directly to the other Settlement System of the Depository.

The securities initially recorded in Clearstream Banking Luxembourg S.A as Issuer CSD can be transferred indirectly between Settlement Systems of the Depository if link arrangement provides so.

After the merger of the three Baltic CSDs, the Depository will only maintain the existing unilateral CSD link arrangements with following foreign CSDs:

- (i) Clearstream LUX²; and
- (ii) Polish CSD.

In the future, the Depository may establish new CSD link arrangements with foreign CSDs, subject to business needs and in compliance with the CSDR and the applicable law.

System design and operations

The Depository uses a common **CSD** System for operation of its Settlement Systems, including for the record keeping, data processing and information exchange, maintaining Estonian Register of Securities and providing other CSD services.

All the Operational Accounts with all the Settlement Systems migrate to T2S Platform on one to one basis, except where the Rulebook expressly provides otherwise. The Depository outsources the validation, matching and settlement of all the transfer orders in T2S eligible securities to T2S. The instructions concerning T2S eligible securities, settlement services and other T2S services are provided in an integrated technical T2S Platform.

The Participants may connect to T2S as indirectly connected parties (“**ICP**”) via CSD System or directly connected parties (“**DCP**”), subject to compliance with the requirements of the Rulebook and T2S functionalities. The settlement instructions are processed according to the following principles:

- (i) a DCP sends instructions directly send to T2S and such instructions are subject to T2S validation, matching and settlement processes only.
- (ii) an ICP sends instructions to CSD System and such instructions are subject to technical and business validation process of CSD System. If the validation by CSD System is successful, the instructions are subject to T2S validation, matching and settlement processes.

Settlement services regarding **T2S eligible securities** are provided in accordance with the Rules which among others implement the requirements of T2S Framework Agreement and T2S functionalities. The following principles apply to settlement of T2S eligible securities:

- (i) all securities accounts with the Settlement Systems of the Depository, and their balances are operated on the T2S Platform, unless expressly stated otherwise in the Rulebook;
- (ii) securities account balances operated on the T2S Platform are changed only in T2S;
- (iii) the moments of entry ("**SF I**") and irrevocability ("**SF II**") of transfer orders into the Settlement Systems of the Depository are defined pursuant to Collective Agreement between, among others, the Eurosystem and the Baltic CSDs;
- (iv) the settlement of transfer orders is effected on a gross basis, considering, among others, the application or availability of the following procedures and features in accordance with T2S Rules and these Rules:
 - (a) technical netting with optimization;
 - (b) DvP settlement against CeBM through DCAs in case of DvP instructions;
 - (c) partial settlement;
 - (d) conditional settlement;
 - (e) tolerance matching;
 - (f) priorities management;
 - (g) hold and release of settlement instructions; and
 - (h) linking of transfer orders.

Settlement services regarding **non-T2S eligible securities** are provided in CSD System in accordance with the Rulebook, applicable law and functionalities of CSD System.

Settlement schedule and processing cycles for T2S eligible securities and for non T2S securities are set out in the Rules and documentation incorporated thereto by reference.

Legal and regulatory framework

Principal laws applicable to the Depository and all the Settlement Systems as amended:

- (i) Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 and delegated legal acts;
- (ii) Laws implementing Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality;⁴
- (iii) Financial Collateral Directive;⁵

⁴ Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems.

Latvian Financial Instruments Market Law which regulates certain aspects of the constitution and supervision of the Depository.

Principal laws applicable to Estonian Settlement System:

- (i) Securities Registry Act (*Väärtpaberite registri pidamise seadus*);
- (ii) Securities Market Act;
- (iii) Commercial Code;
- (iv) Investments Funds Act.

Principal laws applicable to Latvian Settlement System:

- (i) Commercial Law;
- (ii) Financial Instruments Market Law;
- (iii) Law on Settlement Finality in Payment and Financial Instruments Settlement Systems;
- (iv) Financial Collateral Law.

Principal laws applicable to Lithuanian Settlement System:

- (i) Law on Companies;
- (ii) Law on Markets in Financial Instruments;
- (iii) Law on Securities;
- (iv) Law on Banks;
- (v) Law on Settlement finality in Payment and Securities Settlement Systems;
- (vi) Law on Financial Institutions;
- (vii) Law on Collective Investment Undertakings.

Documentation:

- (i) Nasdaq CSD Rulebook and documents incorporated thereto by reference
- (ii) Templates of Nasdaq CSD contractual documents
- (iii) Nasdaq CSD disclosure documents.

Key objectives

Following are the key objectives of the Depository operations:

- a) meet regulatory requirements applicable to its operations, including the uptime requirement of its main production IT systems according to the following service level conditions:
 - (i) downtime does not exceed 2 hours in no more than six occasions per year and
 - (ii) average availability of the systems per annum is at least 99,5%.

⁵ Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements (with amendments).

- b) offer internationally accepted communication procedures, communication standards and wide range of measures and tools that help to prevent settlement fails;
- c) serve its main customer groups (issuers and participants) in a timely fashion (i.e. that correct and complete issuer applications and transfer orders are processed within applicable deadlines);
- d) have settlement failure rates for the securities Settlement Systems operated by the Depository below **0.5 per cent per year**.
- e) maintain its overall risk rating* at level A (i.e. low risk CSD) per Depository Review and Risk Evaluation Service, provided by Thomas Murray Data Services.

III. Detailed principle-by-principle responses allowing conclusions on Depository's observance

PS	CSD	SSS	CCP	TR
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Principle 1: Legal basis

An FMI should have a well-founded, clear, transparent, and enforceable legal basis for each material aspect of its activities in all relevant jurisdictions.

As a robust legal basis for an FMI's activities in all relevant jurisdictions is critical to an FMI's overall soundness, this principle should be reviewed holistically with the other principles.

Key consideration 1: The legal basis should provide a high degree of certainty for each material aspect of an FMI's activities in all relevant jurisdictions.

Material aspects and relevant jurisdictions

Q.1.1.1: *What are the material aspects of the FMI's activities that require a high degree of legal certainty (for example, rights and interests in financial instruments; settlement finality; netting; interoperability; immobilisation and dematerialisation of securities; arrangements for DvP, PvP or DvD; collateral arrangements (including margin arrangements); and default procedures)?*

The Depository provides the following **core CSD services** (involving the following material aspects in those roles):

A) Initial recording of securities in a book entry form in any Settlement System through initial crediting and subsequent crediting and debiting of securities accounts ("notary service"). Material aspects with regard to the notary service include:

- (A1) Registration procedures;
- (A2) Corporate actions management procedures;
- (A3) Rights and interests in financial instruments (legal consequences of registration).

B) Maintaining and providing securities accounts with any Settlement System (i.e. at the top tier level) ("central maintenance service"). Material aspects with regard to the central maintenance service include:

- (B1) Rights and interests in financial instruments (legal consequences of registration);
- (B2) Registration of a pledges or financial collateral over securities.

C) Operating Estonian Settlement System, Latvian Settlement System and Lithuanian Settlement System ("settlement service"). Material aspects with regard to the settlement service include:

- (C1) Settlement finality of securities leg and cash leg;
- (C2) Legal consequences of default and default procedures;
- (C3) Link arrangement with foreign CSDs.

Q.1.1.2: *What are the relevant jurisdictions for each material aspect of the FMI's activities?*

Estonia is the relevant jurisdiction for Estonian Settlement System, Latvia is the relevant jurisdiction for Latvian Settlement System and Lithuania is the relevant jurisdiction for Lithuanian Settlement System respectively for each material aspect listed in 1.1.1 above.

Luxembourg and Poland are the relevant jurisdictions for (C3) where the Depository acts as an Investor CSD as per a link with Clearstream LUX and as Issuer CSD as per link with Polish CSD, respectively.

Q.1.1.3: *How does the FMI ensure that its legal basis (that is, the legal framework and the FMI's rules, procedures and contracts) provides a high degree of legal certainty for each material aspect of the FMI's activities in all relevant jurisdictions?*

Common legal basis for the operation of the Depository and its services is set out in the CSDR and delegated legislation of the European Commission (technical regulatory standards and implementing regulatory standards). Country specific rules in connection with the operation of Settlement Systems are provided in Estonian laws, Latvian laws and Lithuanian laws, as a case may be, including the national laws implementing the European Union (EU) secondary legislation.

In addition to directly applicable EU laws, the principal laws applicable to the **Estonian Settlement System** are:

- 1) Estonian Central Register of Securities Act (“**ECRS Act**”)/ Securities Registry Act (“**SRA**”), available at <https://www.riigiteataja.ee/en/eli/514012015003/consolide>
- 2) Securities Market Act (“**SMA**”), available at <https://www.riigiteataja.ee/en/eli/523112015001/consolide>

In addition to directly applicable EU laws, the principal laws applicable to matters in connection with the **Latvian Settlement System** are:

- 3) Financial Instruments Market Law, available at: <http://likumi.lv/doc.php?id=81995> (unofficial English translation available at http://www.vvc.gov.lv/export/sites/default/docs/LRTA/Likumi/Financial_Instrument_Market_Law.doc);
- 4) Law on Settlement Finality in Payment and Securities Settlement Systems (“**SFD LV**”), available at: <http://likumi.lv/doc.php?id=82434>;
- 5) Financial Collateral Law, available at: <http://likumi.lv/doc.php?id=107799> (unofficial translation in English available at http://www.vvc.gov.lv/export/sites/default/docs/LRTA/Likumi/Financial_Collateral_Law.doc);
- 6) Commercial Law, available at: <http://likumi.lv/doc.php?id=5490> (unofficial English translation available at http://www.vvc.gov.lv/export/sites/default/docs/LRTA/Likumi/The_Commercial_Law.doc).

In addition to directly applicable EU laws, the principal laws applicable to matters in connection with the **Lithuanian Settlement System** are:

- 7) Civil Code, available at: http://www3.lrs.lt/pls/inter3/dokpaieska.rezult_e?p_nr=&p_nuo=&p_iki=&p_org=&p_drus=10&p_kalb_id=2&p_title=civil&p_text=&p_pub=&p_met=&p_lnr=&p_denr=&p_es=0&p_tid=&p_tkid=&p_t=0&p_tr1=2&p_tr2=2&p_gal=&p_rus=1;
- 8) Law on Markets in Financial Instruments, available at: http://www3.lrs.lt/pls/inter3/dokpaieska.rezult_e?p_nr=X-1024&p_kalb_id=2;
- 9) Law on Companies, available at: http://www3.lrs.lt/pls/inter3/dokpaieska.rezult_e?p_nr=VIII-1835&p_kalb_id=2;
- 10) Law on Settlement Finality in Payment and Securities Settlement Systems (“**SFD LT**”), available at: http://www3.lrs.lt/pls/inter3/dokpaieska.showdoc_1?p_id=276063.

The Depository can, to a limited extent, control and influence the degree of legal certainty through its rules, procedures and contracts with the participants and issuers. According to the assessment of

Depository's legal services above provides a high degree of legal certainty for each material aspect of the Depository's activities in all relevant jurisdictions. This assessment has been confirmed by legal opinion that will be provided at the beginning of 2017 from external law firm.

- a) *For an FMI that is a CSD, how does the CSD ensure that its legal basis supports the immobilisation or dematerialisation of securities and the transfer of securities by book entry?*

The Depository records securities in any Settlement System in book entry form subsequent to direct issuance in dematerialised form in accordance with:

- (i) Article 3 of CSDR (applies to all the Settlement Systems);
- (ii) the Law of Obligations Act of Estonia (applies to Estonian Settlement System);
- (iii) the Financial Instrument Market Law of Latvia and the Commercial Law of Latvia (applies to Latvian Settlement System);
- (iv) the Law on Companies of Lithuania and the Law on Markets in Financial Instruments of Lithuania (applies to Lithuanian Settlement System);
- (v) the Rules.

The Depository may also record physical securities in any Settlement System in book entry form after their immobilisation with the Depository in accordance with Article 3 of the CSDR and the procedure set out in the agreement between the Depository, on the one hand, and the Issuer or the owner of securities, on the other hand (Section 4 of Chapter I of the Rules).

Securities registered with any Settlement System may be transferred only in book entry form.

- b) *For an FMI that is a CCP, how does the CCP ensure that its legal basis enables it to act as a CCP, including the legal basis for novation, open offer or other similar legal device? Does the CCP state whether novation, open offer or other similar legal device can be revoked or modified? If yes, in which circumstances?*

Not applicable.

- c) *For an FMI that is a TR, how does the TR ensure that its legal basis protects the records it maintains? How does the legal basis define the rights of relevant stakeholders with respect to access, confidentiality and disclosure of data?*

Not applicable.

- d) *For an FMI that has a netting arrangement, how does the FMI ensure that its legal basis supports the enforceability of that arrangement?*

Not applicable.

- e) *Where settlement finality occurs in an FMI, how does the FMI ensure that its legal basis supports the finality of transactions, including those of an insolvent participant? Does the legal basis for the external settlement mechanisms the FMI uses, such as funds transfer or securities transfer systems, also support this finality?*

Common rules applicable to all Settlement Systems

Chapter I of the Rules provides common rules on settlement services that apply to all the Settlement Systems. Provisions of Chapter I of the Rules clearly define the settlement finality moments (SF I and SF II) of securities transfer orders in compliance with the Collective Agreement concluded between, among others, the Eurosystem and the three Baltic CSDs and standards and procedures developed by T2S and the national laws implementing the Settlement Finality Directive. The Rules also clearly define the settlement finality moment (SF III) for the securities transfer.

Settlement finality moments are harmonised for T2S eligible securities and non T2S eligible securities, subject to T2S and CSD System functionalities. Any settlement finality moment (SFI, SF II and SF III) in the securities account is deemed to occur:

- (i) in case of T2S eligible securities, when T2S assigns a 'time stamp' in accordance with T2S Rules, regardless of whether the securities account records in CSD System have been synchronised with T2S data; or
- (ii) in case of non-T2S eligible securities, when CSD System assigns a 'time stamp' in accordance with technical module of CSD System.

As long as counterparty risk is concerned (counterpart fails to deliver) following common principles apply:

- (i) the Depository executes the settlement on the basis of transfer orders only if sufficient funds and securities are available.
- (ii) the Depository itself does not maintain any guarantee fund or similar mechanism. However, guarantee fund is maintained by the operator of the Baltic Stock Exchange to address settlement fails in case of event of default by a Participant.
- (iii) settlement date will be postponed if the transaction fails to settle on ISD.

The Rules provide the following measures to address settlement failures:

- (i) the Depository imposes penalties on the Participant failing to deliver securities on the ISD, distributes such amounts to the Participants suffering from the failed deliveries and reports to the competent authorities in compliance with the CSDR technical standards on settlement discipline from the date when such standards become effective;
- (ii) the Depository initiates buy-in in case the failing Participant does not deliver securities during the extension period in compliance with the CSDR technical standards on settlement discipline from the date when such standards become effective;
- (iii) the Participant may use auto-collateralisation through T2S service, if it has such contract with Central Banks, in order to cover a lack of cash for securities transaction settlement in accordance with Central Bank regulations and T2S Rules.

In case the insolvency proceedings of a Settlement System Participant are commenced, the existing and new transfer orders of the insolvent System Participant are handled according to the Depository's Default Rules set out in Annex II to the Rules.

With respect to cash leg for non-T2S eligible securities registered with the Settlement System in euros, Section 6 of Chapter I of the Rules clearly define the finality of the cash transfers between CSAs in CSD System (i.e. sub-bookkeeping records with CSD System). Finality moments for the transfer of cash in T2 Component System are governed by the rules and procedures of the respective T2 Component System.

Latvian Settlement System

Articles 8 to 10 of SFD LV implementing Settlement Finality Directive provide the statutory framework for the settlement finality in the Latvian Settlement System. In particular, Latvian Settlement System rules must provide:

- (i) the entry moment of a transfer order in the system (SF I) (*Article 8(4) of the SFD LV*); and

- (ii) the moment after which the transfer order is irrevocable (SF II) (*Article 10(1) of the SFD LV*).

In case of the Participant's insolvency Latvian law provides, among others, the following safeguards:

- (i) the Depository as an operator of the Latvian Settlement System, upon being notified that the operations of a System Participant are suspended and/or bankruptcy proceedings are initiated against it, take all measures to prevent transfer orders submitted to the Latvian Settlement System by that participant from being entered into the Latvian Settlement System;
- (ii) transfer orders and netting shall be legally enforceable and binding on third parties even in the event of insolvency proceedings opened against a participant, provided that transfer orders were entered into the Latvian Settlement System (SFI) before the moment of opening of such insolvency proceedings (*Article 8(1) of the SFD LV*);
- (iii) where the transfer orders are entered into the Latvian Settlement System (SFI) after the moment of opening of insolvency proceedings and are executed within the business day, during which the opening of such proceedings occur, they shall be legally enforceable and binding on third parties only if, at the time that such transfer orders become irrevocable (SF II), the Depository was neither aware, nor should have been aware, of the opening of such proceedings (*Article 8(2) of the SFD LV*).

Provisions regarding SF I (moment of entry), SF II (moment of irrevocability) and SF III (finality of settlement) are provided in the Chapter I of the Rules (section 6.4, 6.5. and 6.6. respectively).

Estonian Settlement System

Paragraphs 212 - 229 of the SMA implementing SFD in Estonia provide statutory framework for the operation of Estonian Settlement System. Under Point 9 of § 222 of the SMA the Estonian Settlement System rules need to stipulate the conditions determining the settlement finality, including the moment of receipt of the transfer order (SF I) and the moment of irrevocability of transfer order (SF II).

In case of Participant's insolvency Estonian law provides, among others, the following safeguards:

- (i) the Depository as an operator of Estonian Settlement System shall immediately stop accepting transfer orders from the insolvent Participant to the Estonian Settlement System pursuant to the procedure prescribed in the Estonian Settlement System rules (*§ 228 (1) of the SMA*);
- (ii) transfer instructions entered into the system by the Participant (SF I) prior to opening of the insolvency proceedings shall be settled if that is possible considering the free balances on respective accounts on the basis of § 228 (2) of the SMA. The same shall apply to transfer orders submitted on the day of initiation of the insolvency proceedings provided that the Depository was not and did not have to be aware of the initiation of such proceedings. No settlement will be effected in case of insufficiency of balances. The registrar of the Estonian Register of Securities, while it is operating as an operator of a securities settlement system, does not have the right to guarantee the performance of claims and obligations arising on the basis of transfer orders (*§ 272 (2) of the SMA*).
- (iii) if the transfer orders are forwarded to the Estonian Settlement System and executed in accordance with the Estonian Settlement System rules on the business day of the initiation of the insolvency proceedings of the System Participant, they shall be valid only if the Depository was neither aware, nor should have been aware, of the opening of such proceedings (*§ 228 (3) of the SMA*).

Lithuanian Settlement System

SFD LT provides that the Depository's Rules must provide:

- (i) the moment of entry of settlement instructions and payment orders into the Lithuanian Settlement System (SF I) (*Article 4(3)(3) of the SFD LT*); and
- (ii) the moment after which the settlement instruction or the payment order admitted to the system may not be revoked (SF II) (*Article 4(3)(4) of the SFD LT*).

In case of the Participant's insolvency Lithuanian law provides, among others, the following safeguards:

- (i) the Depository as an operator of the Lithuanian Settlement System, upon being notified that the operations of a System Participant are suspended and/or bankruptcy proceedings are initiated against it, take all measures to prevent transfer orders submitted to the Lithuanian Settlement System by that participant from being entered into the Lithuanian Settlement System (*Article 7(3) of SFD LT*);
- (ii) transfer orders and netting shall be legally enforceable and binding on third parties even in the event of insolvency proceedings opened against a participant, provided that transfer orders were entered into the Lithuanian Settlement System (SFI) before the moment of opening of such insolvency proceedings (*Article 7(1) of the SFD LT*);
- (iii) if the transfer orders are entered into the Lithuanian Settlement System (SFI) after the moment when the operations of the System Participant were suspended and/or bankruptcy proceedings were initiated against it and are executed within the business day, during which the suspension of operations and/or initiation of bankruptcy proceedings, they shall be valid and not disputed by third parties only if, after the time of settlement, the Depository can prove that it was neither aware, nor should have been aware, of the suspension of operations and/or the initiation of the bankruptcy proceedings (*Article 7(4) of SFD LT*).

In case of a default of a participant, the Depository or the clearing bank acts in compliance with the legal acts regarding settlement of central market and OTC transactions. In case the activities of a Participant were are suspended temporarily or irrevocably by a decision of the Bank of Lithuania or other competent authority, default management procedure set out in the Depository's Rules is applicable.

Key consideration 2: An FMI should have rules, procedures, and contracts that are clear, understandable, and consistent with relevant laws and regulations.

Q.1.2.1: *How has the FMI demonstrated that its rules, procedures and contracts are clear and understandable?*

We consider that *inter alia* the following demonstrates and proves that rules, operational model, procedures and contracts of the Depository are clear and understandable:

1. extensive consultations with all the relevant stakeholders, including the Participants, regulators, central banks and representatives of ECB were carried out prior to the adoption of the operational model and rules supporting it;
2. the fact that relevant sections of the Depository's Rules are subject to prior consultations with the FCMC and
 - (i) in case of Latvian Settlement System rules, opinion of the Bank of Latvia,
 - (ii) in case of the Estonian Settlement System rules, approval by the Estonian FSA; and
 - (iii) in case of the Lithuanian Settlement System, approval by the Bank of Lithuania (see the response under Q.1.2.3 below);
3. the fact that the Depository is supervised by FCMC as a home Member State supervisor, the Estonian FSA and the Bank of Lithuania as host Member State supervisors;

4. the fact that the Estonian Settlement System is subject to oversight by Bank of Estonia, the Latvian Settlement System is subject to oversight by the Bank of Latvia and the Lithuanian Settlement System is subject to oversight by the Bank of Lithuania;
5. the fact that rules, contracts and key procedures are subject to mandatory review and approval of the in-house representative of the Office of General Counsel (Nasdaq's cross-organisational unit of international legal counsels and compliance experts); and
6. the fact that Office of General Counsel has been assigned the responsibility for keeping rules and contracts up to date and consistent with relevant laws;
7. the fact that Rules of the Depository, as well as its standard contracts and non-classified procedures are made public through its website.

Q.1.2.2: *How does the FMI ensure that its rules, procedures and contracts are consistent with relevant laws and regulations (for example, through legal opinions or analyses)? Have any inconsistencies been identified and remedied? Are the FMI's rules, procedures and contracts reviewed or assessed by external authorities or entities?*

Please refer to the response to the Q.1.2.1. Further, the Depository may request (on regular or ad hoc basis) an independent legal opinion to validate that specific aspects of its Rules, procedures or contracts are consistent with relevant laws and regulations. *Ad hoc* requests would be triggered by cases or situations (e.g. customer complaints) that put consistency under question.

Q.1.2.3: *Do the FMI's rules, procedures and contracts have to be approved before coming into effect? If so by whom and how?*

Latvia

The Depository Rules and amendments thereto have to be approved by Depository's Supervisory Council.

In case the rules deal with Latvian Settlement System, the FCMC takes a decision on the designation of the Latvian Settlement System as a securities settlement system within the meaning of the Settlement Finality Directive only after obtaining an opinion of the Bank of Latvia regarding the compliance of the Latvian Settlement System and its rules with the SFD LV (*Section 19 of the SFD LV*).

Estonia

The Estonian Settlement System rules and amendments thereto require approval of the Estonian FSA pursuant to § 223 of the SMA. The application for the approval of the Estonian Settlement System rules should be accompanied by explanations and evaluation of their impact on the members of the system and on the operation of the Estonian Settlement System.

Lithuania

The Lithuanian Settlement System rules and amendments thereto require registration of this system with the Bank of Lithuania pursuant to Article 5 of the SFD LT.

Procedures and contracts

Under Estonian, Latvian and Lithuanian law it is not necessary to obtain approval of procedures and contracts from the competent authorities.

Key consideration 3: An FMI should be able to articulate the legal basis for its activities to relevant authorities, participants, and, where relevant, participants' customers, in a clear and understandable way.

Q.1.3.1: *How does the FMI articulate the legal basis for its activities to relevant authorities, participants and, where relevant, participants' customers?*

It is contemplated that the Depository will publish on its website the following information in relation to the legal basis of its key roles and activities:

1. statement that the Depository acts as a CSD authorised under the CSDR to provide core CSD services and certain non-banking-type ancillary services of CSDs (i) in Latvia through its Latvian head office, (ii) in Estonia through its Estonian branch and (iii) in Lithuania through its Lithuanian branch;
2. statement that the Depository acts as an operator of the Estonian Settlement System on the basis and in accordance with the relevant provisions (§ 212-229) of the SMA and CSDR;
3. statement that the Depository acts as an operator of the Latvian Settlement System in accordance with the Financial Instruments Market Law, SFD LV and CSDR;
4. statement that the Depository acts as an operator of the Lithuanian Settlement System on the basis and in accordance with the Law on Markets in Financial Instruments, SFD LT and CSDR.

In addition to the above the Depository will publish on its website:

- a) general information about the Depository;
- b) Rules of the Depository;
- c) references to the applicable legal acts.

Key consideration 4: An FMI should have rules, procedures, and contracts that are enforceable in all relevant jurisdictions. There should be a high degree of certainty that actions taken by the FMI under such rules and procedures will not be voided, reversed, or subject to stays.

Enforceability of rules, procedures and contracts

Q.1.4.1: *How does the FMI achieve a high level of confidence that the rules, procedures and contracts related to its operations are enforceable in all relevant jurisdictions identified in key consideration 1 (for example, through legal opinions and analyses)?*

As noted in under Q. 1.2.1, Rules, contracts and key procedures are subordinated to mandatory review and approval of the Office of General Counsel. Further, the Depository may request (*on regular or ad hoc basis*) an independent legal opinion to validate that specific aspects of its Rules, procedures or contracts are enforceable in relevant jurisdictions. *Ad hoc* requests would be triggered by cases or situations (e.g. customer complaints) that put enforceability under question.

The Depository's rules, procedures and contracts are enforceable in Estonia, Latvia or Lithuania. The Depository does not offer a possibility to directly transfer securities across the Settlement Systems, and the account holders may access securities registered with the Settlement System only via a Participant of the respective Settlement System. In case of cross-border settlement of securities registered with Clearstream LUX as Issuer CSD, the settlement of a transfer order within the settlement system operated by Clearstream LUX is subject to the law of Luxembourg.

Q.1.4.2: *How does the FMI achieve a high degree of certainty that its rules, procedures and contracts will not be voided, reversed or subject to stays? Are there any circumstances in which an FMI's actions under its rules, procedures or contracts could be voided, reversed or subject to stays? If so, what are those circumstances?*

To the best of our knowledge, there are no circumstances in which Depository's actions under its rules, procedures or contracts could be voided, reversed or subject to stays.

Q.1.4.3: *Has a court in any relevant jurisdiction ever held any of the FMI's relevant activities or arrangements under its rules and procedures to be unenforceable?*

No.

Key consideration 5: An FMI conducting business in multiple jurisdictions should identify and mitigate the risks arising from any potential conflict of laws across jurisdictions.

Q.1.5.1: *If the FMI is conducting business in multiple jurisdictions, how does the FMI identify and analyse any potential conflict-of-laws issues? When uncertainty exists regarding the enforceability of an FMI's choice of law in relevant jurisdictions, has the FMI obtained an independent legal analysis of potential conflict-of-laws issues? What potential conflict-of-laws issues have the FMI identified and analysed? How has the FMI addressed any potential conflict-of-laws issues?*

Measures to address conflict of laws issues

Operational model

The operational model of the Depository is designed with a view to limit potential conflict of laws issues. In particular, there are no settlement links or direct cross-border transfers between Settlement Systems operated by the Depository. Securities initially recorded in one Settlement System of the Depository, or transferred to such Settlement System from Issuer CSD, cannot be transferred directly to the other Settlement System of the Depository. In order to access securities registered with one or more Settlement Systems, the party wishing to hold such securities has to become a Participant itself or use a Participant of that System. In case a foreign legal entity requests the right of participation to the Depository, the Depository may request the applicant to provide a reasoned and independent legal opinion from a reputable law firm or attorney-at-law in the form and substance acceptable to the Depository establishing that possible conflict of laws issues would not impede the enforceability of the Rules and ability of the applicant to meet its obligations as in connection with its participation in the Settlement System(s).

As a general rule, securities constituted under Estonian, Latvian or Lithuanian law will be admitted to the Settlement System governed by the same law (e.g. shares of companies registered in Latvia and other securities constituted under Latvian law are admitted to Latvian Settlement System). However, the Depository may also admit securities of a foreign Issuer to any Settlement System, subject to compliance by the Issuer with the admission criteria set out in the Rules and requirements and compliance by the Depository with Articles 23(3)(e) and 49 of the CSDR. In case a foreign Issuer requests to admit its securities to any Settlement System, the Depository may request the applicant to provide a reasoned and independent legal opinion from a reputable law firm or attorney-at-law in the form and substance acceptable to the Depository establishing that possible conflict of laws issues will not jeopardize the compliance by the Issuer with the admission criteria provided in the Rules.

Rules on applicable law

The Rules clearly define the law applicable to various aspects of the Depository's operations in compliance with the CSDR, Settlement Finality Directive, Financial Collateral Directive and national laws.

Rules on dispute resolution

The provisions on dispute resolution are aligned with the provisions on the applicable law to ensure, to the extent possible, that the dispute is settled by the court of the country whose law applies to the subject matter (e.g. Latvian court has jurisdiction over disputes regarding the rights and obligations of the Participant to the Latvian Settlement System, regardless of whether such Participant is established in Latvia, Estonia or Lithuania) (see Section “General provisions” of Chapter I of the Rulebook)

Monitoring of risks

The Depository has designed link-specific risk assessment procedure on annual basis to ensure that various risks, including those that may be due to elements of another jurisdiction, are at acceptable level. This includes analysis of annual risk-assessment questionnaires.

Law applicable to Settlement Systems and entitlement to securities

Securities registered with the Depository as Issuer CSD

The Estonian Settlement System and the rights and obligations of the Depository against the Participant and *vice versa*, acting as a System Participant of the Estonian Settlement System, in respect of the matters listed in the Rulebook are governed by Estonian law.

The Latvian Settlement System and the rights and obligations of the Depository against the Participant, acting as a System Participant of the Latvian Settlement System, in respect of the matters listed in the Rulebook are governed by Latvian law

The Lithuanian Settlement System and the rights and obligations of the Depository against the Participant, acting as a System Participant of the Lithuanian Settlement System, in respect of the matters listed in the Rulebook are governed by Lithuanian law.

In order to facilitate legal certainty as to the ambit of the legal perimeter of the respective Securities Settlement System, the Rules provide for a catalogue of matters that are governed by the law applicable to the Settlement System, which *inter alia* include:

- (i) the legal nature and effects resulting from a credit or other entries to a securities account (e.g. the entitlement to securities held by a Latvian credit institution in Estonian Settlement System is governed by Estonian law) (*Estonian Private International Law Act*);
- (ii) the legal nature and the requirements of an acquisition or disposition of securities as well as its effects between the parties and against third parties, including the effects of settlement finality moments of transfer orders entered into the Settlement System (*national laws implementing Article 2(a) of the Settlement Finality Directive*);
- (iii) the legal nature of pledge or financial collateral, the requirements for perfection and provision of securities, pledge or financial collateral arrangement relating to book-entry securities pledge or financial collateral, and requirements necessary to render such an arrangement and provision effective against third parties (*for financial collateral see Article 9(2) of the Settlement Finality Directive and Article 9 of the Financial Collateral Directive, Article 16 of SFD LV, Article 9(2) and (3) of SFD LT, Article 231 of the Estonian Private International Law Act*);
- (iv) in case of insolvency proceedings of the System Participant are commenced, the rights and obligations arising from, or in connection with, the participation of that System Participant in the Settlement System (e.g. in case insolvency proceedings of a Latvian credit institution that is a Participant to Lithuanian Settlement System are commenced, the rights and obligations arising from, or in connection with, the participation of a Latvian credit institution in such Settlement System are governed by Lithuanian law (*Article 8 of the Settlement Finality Directive and Article 24 of the Bank Winding-up Directive, Article 15 of SFD LV, Article 8(5) and (6) of the SFD LT*).

Securities held by the Depository as Investor CSD

Foreign Securities registered with a foreign CSD as an Issuer CSD that are held by the holder of securities account with the Settlement System operated by the Depository via a CSD link arrangement are held with the Default Settlement System associated with the respective Operational Account. The Default Settlement System of the Operational Account is the Default Settlement System of the Account Operator that has requested to open the respective Operational Account, unless the Account Operator has selected a different Default Settlement System in the application to open a new Operational Account. For instance, in case a Participant to two or three Settlement Systems has designated Latvian Settlement System as a Default Settlement System and such Participant acquires securities registered with Clearstream LUX as Issuer CSD, the securities will be deemed to be held in Latvian Settlement System and, hence, proprietary aspects of such holdings will be subject to Latvian law.

The Depository agrees with each foreign CSD on the law applicable to contractual relationship and obtains a legal opinion from the local legal counsel.

Rights and obligations of the Issuer

The provisions of the Rules regarding the rights and obligations of the Depository against the Issuer and *vice versa* are governed by the law which applies to the Settlement System in which respective securities of the Issuer are recorded, unless the Rules or the applicable conflict of laws provide otherwise.

Corporate actions

Corporate actions with respect to securities registered with any Settlement System are executed according to the law under which the securities are constituted (e.g. in case of shares, the law of the country where the Issuer is registered).

Other matters

The provision of other CSD services and the rights and obligations of the Depository against the Participant are governed by Latvian law, unless the Rules (i.e. provisions dealing with Settlement Systems, the rights and obligations of the Issuer, corporate actions) or the applicable conflict of laws provide otherwise. This includes any other matter not expressly covered by the Rules, such as the right of the Depository to impose late payment interest for delayed payment of the participation fee.

PS	CSD	SSS	CCP	TR
•	•	•	•	•

Principle 2: Governance

An FMI should have governance arrangements that are clear and transparent, promote the safety and efficiency of the FMI, and support the stability of the broader financial system, other relevant public interest considerations, and the objectives of relevant stakeholders

In reviewing this principle, it should be noted that if an FMI is wholly owned or controlled by another entity, the governance arrangements of that entity should also be reviewed to ensure that they do not have adverse effects on the FMI's observance of this principle. As governance provides the processes through which an organisation sets its objectives, determines the means for achieving those objectives and monitors performance against those objectives, this principle should be reviewed holistically with the other principles.

Key consideration 1: An FMI should have objectives that place a high priority on the safety and efficiency of the FMI and explicitly support financial stability and other relevant public interest considerations.

Q.2.1.1: *What are the FMI's objectives, and are they clearly identified? How does the FMI assess its performance in meeting its objectives?*

The Depository's primary objective is to provide CSD services to its participants, issuers and other stakeholders and thereby support safe and robust functioning of the securities market.

Following are the key objectives of the Depository operations:

- a) meet regulatory requirements applicable to its operations, including the uptime requirement of its main production IT systems according to the following service level conditions:
 - (i) downtime does not exceed 2 hours in no more than six occasions per year and
 - (ii) average availability of the systems per annum is at least 99,5%.
- b) offer internationally accepted communication procedures, communication standards and wide range of measures and tools that help to prevent settlement fails;
- c) serve its main customer groups (issuers and participants) in a timely fashion (i.e. that correct and complete issuer applications and transfer orders are processed within applicable deadlines);
- d) have settlement failure rates for the securities Settlement Systems operated by the Depository below **0.5 per cent per year**.
- e) maintain its overall risk rating* at level A (i.e. low risk CSD) per Depository Review and Risk Evaluation Service, provided by Thomas Murray Data Services.

As a matter of general business strategy the Depository intends to maintain a very low risk profile by limiting its activities to core CSD services and certain non-banking type ancillary services that do not entail credit and liquidity risks.

The assessment of meeting the above objectives is made as follows:

- (i) the Depository performs at least annual internal assessment of meeting its key objectives as part of its regular risk self-assessment procedure;
- (ii) under Article 22(1) of the CSDR the FCMC at least on an annual basis performs external assessment by reviewing the arrangements, strategies, processes and mechanisms implemented by the Depository with respect to compliance with the CSDR and by evaluating the risks to which the Depository is, or might be, exposed or which it creates for the smooth functioning of securities markets. The FCMC may withdraw the authorisation in circumstances stipulated in Article 20(1) of the CSDR.

Q.2.1.2: *How do the FMI's objectives place a high priority on safety and efficiency? How do the FMI's objectives explicitly support financial stability and other relevant public interest considerations?*

Please refer to the response provided under Q.2.1.1 above.

Key consideration 2: An FMI should have documented governance arrangements that provide clear and direct lines of responsibility and accountability. These arrangements should be disclosed to owners, relevant authorities, participants, and, at a more general level, the public.

Governance arrangements

Q.2.2.1: *What are the governance arrangements under which the FMI's board of directors (or equivalent) and management operate? What are the lines of responsibility and accountability within the FMI? How and where are these arrangements documented?*

The Depository will operate in the form of Societas Europaea within the meaning of the SE Regulation. According to the Commercial law of Latvia and articles of association the Depository has the following managing bodies.

General shareholder meeting

The Depository is 100% owned subsidiary of Nasdaq Nordic Ltd, a stock exchange holding company in Finland. Nasdaq Nordic Ltd through a chain of holding companies is fully owned by the Nasdaq Inc., a company incorporated in Delaware, U.S.A.

Supervisory Council

Supervisory Council represents the interest of the shareholder between shareholder meetings, supervises the activities of the Management Board in accordance with the articles of association and performs other functions provided in Latvian law. The responsibility of the Supervisory Council is set out in the Commercial Law of Latvia, Latvian Financial Instruments Market Law and Depository's articles of association.

Management Board

Management Board is responsible for day-to-day management of the Depository. The responsibility of the Management Board is set out in the Commercial Law of Latvia, Financial Instruments Market Law of Latvia and Depository's articles of association.

Committees

The Depository intends to establish User Committee for each Settlement System, risk committee, a remuneration committee and an audit committee in compliance with the CSDR and its technical standards.

The **User Committee** exercises oversight, in an advisory role, over the activities of the Depository which the User Committee considers to be key issues that impact the issuers and participants of the respective Settlement System. The User Committee advises the Supervisory Board on key arrangements that have impact on participants of the Settlement System, the criteria for admission of issuers or participants to the Settlement System, the service level of Depository and other matters which may have impact on participants of the Settlement System.

The authority of:

- (i) the User Committee of the **Estonian Settlement System** is set out in the CSDR and the Rules of Procedure of the User Committee of the Estonian Settlement System;
- (ii) the User Committee of the **Latvian Settlement System** is set out in the CSDR, Latvian Financial Instruments Market Law and the Rules of Procedure of the User Committee of the Latvian Settlement System;
- (iii) the User Committee of the **Lithuanian Settlement System** is set out in the CSDR and the Rules of Procedure of the User Committee of the Lithuanian Settlement System.

Please refer to Chapter II, sub-chapter "Organisation, supervisory and oversight framework of the FMI" on the responsibilities of Risk committee, Audit committee and Remuneration committee.

Reporting lines

Nasdaq Group has brought its Baltic regulated entities (the Depository, operators of Baltic regulated markets and Operational Centre) into regional business organisation “Baltic Market”. Thus, functional and managerial reporting lines aim at efficiency and consolidated regional view.

Further, certain group committees formed by Nasdaq (e.g. Regulatory Capital Committee) and global functions (such as Internal Audit, Global Risk Management, Office of General Counsel and Compliance etc.) take the broader view at Nasdaq operations in the region and have the responsibility of ensuring that Nasdaq regulated entities, including the Depository, comply with applicable regulatory requirements (e.g. capital requirements).

Local lines of responsibility and accountability within the Depository are based on a simple model whereby Business and support units report to the Management Board. Managerial decisions requiring collective approval are adopted by the Management Board.

The Depository maintains a risk management function, compliance and internal control function and an audit function that is separate from other functions. The chief risk officer, the chief compliance officer and the internal control and audit function each has to have separate reporting line to the Management Board and direct access to the Supervisory Council in compliance with the CSDR and its draft regulatory technical standards.

Reporting lines within the legal organization of Depository are set out in Annex 1 ("Organizational Structure and Reporting Lines of Nasdaq CSD SE").

Q.2.2.2: *For central bank-operated systems, how do governance arrangements address any possible or perceived conflicts of interest? To what extent do governance arrangements allow for a separation of the operator and oversight functions?*

Not applicable.

Q.2.2.3: *How does the FMI provide accountability to owners, participants and other relevant stakeholders?*

According to the the Latvian Financial Instruments Market Law the Supervisory Council of the Depository is responsible for providing overview of its activities to shareholders, employees, users and other relevant stakeholders. Under the Latvian Commercial Law the Management Board and the Supervisory Council are accountable to the shareholder for meeting the objectives and financial targets through reporting to the shareholder.

The Depository regularly consults with its participants through the User Committees and other forums (e.g. round tables and consultations) in all matters of material importance (e.g. amending of rules, introduction of new services). Under the CSDR and RTS the Depository has to share independent audit results with the User Committee where:

- (i) such findings relate to the mandate of the User Committee, in particular in key arrangements that impact the users of the Depository;
- (ii) findings may impact the level of provision of services by the Depository.

Disclosure of governance arrangements

Q.2.2.4: *How are the governance arrangements disclosed to owners, relevant authorities, participants and, at a more general level, the public?*

All key elements regarding Depository's governance are publicly disclosed:

Description of the Nasdaq and its ownership in the Baltic financial market infrastructure entities is available at: <http://www.nasdaqbaltic.com/en/exchange-information/about-us/>.

Depository's articles of association will be available at official website of the Depository as of formation of Depository.

Composition of the management bodies will be available at official website of the Depository as of formation of the Depository.

Key consideration 3: The roles and responsibilities of an FMI's board of directors (or equivalent) should be clearly specified, and there should be documented procedures for its functioning, including procedures to identify, address, and manage member conflicts of interest. The board should review both its overall performance and the performance of its individual board members regularly.

Roles and responsibilities of the board

Q.2.3.1: *What are the roles and responsibilities of the FMI's board of directors (or equivalent), and are they clearly specified?*

Supervisory Council represents the interest of the shareholder between shareholder meetings, supervises the activities of the Management Board in accordance with the articles of association and performs other functions provided in Latvian law. The Supervisory Council has two independent members (see the responses provided under Q.2.4.3 and Q.2.4.4 below). In addition to general responsibilities provided in the Latvian Commercial Law and articles of association, under the Latvian Financial Instruments Market Law the Supervisory Council is responsible for:

- (i) establishing procedures by which the management bodies and committees operate;
- (ii) establishing and adopting remuneration policies;
- (iii) ensuring the set-up and the surveillance of the risk management function and the taking of material risk decisions;
- (iv) enabling the independence and adequate resources of risk management, IT, compliance and internal control functions and internal audit;
- (v) monitoring receipt of outsourcing services;
- (vi) monitoring and ensuring compliance with the regulatory requirements and FCMC's instructions;
- (vii) providing overview of its activities to shareholders, employees, users and other relevant stakeholders;
- (viii) approving internal audit plan; and
- (ix) regular reviewing of governance procedures of the Depository.

Further, considering article 49 of the RTS on CSD Requirements (*"Responsibilities of key personnel in respect to the risks referred to in Article 26(1) of Regulation (EU) No 909/2014"*) the Supervisory Council assumes also the following responsibilities:

- (i) establish well-documented policies, procedures and processes by which the Supervisory Council, Management Board and any committees shall operate;
- (ii) establish clear objectives and strategies for the Depository;
- (iii) effectively monitor Management Board;

- (iv) establish adequate remuneration policies;
- (v) ensure the set-up and the surveillance of the risk management function and the taking of material decisions related to risk management;
- (vi) ensure the independence and adequate resources of the risk management function, technology function, compliance and internal control function and internal audit function;
- (vii) be accountable to shareholders or other owners, employees, users and other relevant stakeholders.

The Management Board is responsible for day-to-day management of the Depository. In addition to general responsibilities provided in the Latvian Commercial Law and articles of association, under Article 96 of the Latvian Financial Instruments Market Law the Management Board is responsible for:

- (i) recording of securities with the Depository;
- (ii) admission, suspension and termination of the participation right;
- (iii) regular but not later than once a year reviewing the quality of the services provided to financial market participants and, where necessary, implementing the improvements;
- (iv) ensuring publishing of the Depository's annual financial statement on the Depository's web site;
- (v) ensuring publishing of the information on the Depository's risk management methods and risk management policies on the Depository's web site;
- (vi) preparing Depository's rules and services tariffs and submits for the approval by the Supervisory Council of the Depository;
- (vii) regular reviewing of the efficiency of the Settlement System;
- (viii) ensuring compliance of the Depository's operations with the strategy and objectives set by the Supervisory Council;
- (ix) establishing risk management, IT, compliance and internal control procedures which facilitate achieving the objectives of the Depository;
- (x) ensuring adequate resources for risk management, IT, compliance and internal control functions and internal audit.

Further, considering article 49 of the RTS on CSD Requirements (*"Responsibilities of key personnel in respect to the risks referred to in Article 26(1) of Regulation (EU) No 909/2014"*) the Management Board has to subject the risk management, technology, compliance and internal control procedures to regular review and testing.

Q.2.3.2: *What are the board's procedures for its functioning, including procedures to identify, address and manage member conflicts of interest? How are these procedures documented, and to whom are they disclosed? How frequently are they reviewed?*

Board procedures are provided in the Depository's internal policies and procedures.

The Depository will maintain and operate effective written and administrative arrangements to identify and manage potential conflicts of interests between itself, including its managers, employees, members of the management body or any person directly or indirectly linked to them, and its participants or their clients in compliance with Article 26(3) of the CSDR. The Depository will also maintain and implement resolution procedures where possible conflicts of interest occur.

The CSD LV application for authorisation will contain the following information on the policies and procedures put in place to identify and manage conflicts of interest:

- (i) policies and procedures with respect to the identification, management and disclosure of conflicts of interest and a description of the process used to ensure that the relevant persons are aware of the policies and procedures and any other measures and controls put in place to ensure the requirements on conflicts of interest management are met;
- (ii) resolution procedures whenever possible conflicts of interest occur;
- (iii) arrangements that the CSD LV makes to structure itself and to allocate responsibility for decisions so that it can continue to take proper regulatory decisions notwithstanding any conflicts of interest, including:
 - (a) the size and composition of the Supervisory Council and Management Board and relevant committees;
 - (b) the roles and responsibilities of key individuals, especially where they also have responsibilities in other organisations;
 - (c) the arrangements made to ensure that individuals who may have a permanent conflict of interest in certain circumstances are excluded from the process of taking decisions (or receiving information) about matters in which that conflict of interest would be relevant;
 - (d) an up-to-date register, at the time of the application, of existing material conflicts of interest in relation to any services provided by the applicant CSD and a description of how these are being managed.

The application of CSD LV for authorisation will include a declaration of any potential conflicts of interests that the members of the Supervisory Council and the Management Board may have in performing their duties and how these conflicts are managed in compliance with the RTS.

Furthermore, any Management Board and Supervisory Council member is bound by Global Nasdaq Code of Ethics and Compliance Programme that includes, among others, the requirement to avoid conflicts of interest or, if it is no possible, report conflicts of interest to the global Ethics Team. These procedures are documented and provided in the Nasdaq Code of Ethics.

Q.2.3.3: *Describe the board committees that have been established to facilitate the functioning of the board. What are the roles, responsibilities and composition of such committees?*

The Supervisory Council will establish a User Committee for each Settlement System, an audit committee, a remuneration committee and a risk committee. For information about the committees see information provided under Q. 2.2.1 above.

Review of performance

Q.2.3.4: *What are the procedures established to review the performance of the board as a whole and the performance of the individual board members?*

Depository's members of the Management Board are subject to Nasdaq target setting and performance evaluation and appraisal system. It provides well documented procedures to review the performance of each individual member of the Management Board.

Key consideration 4: The board should contain suitable members with the appropriate skills and incentives to fulfil its multiple roles. This typically requires the inclusion of non-executive board member(s).

Q.2.4.1: *To what extent does the FMI's board have the appropriate skills and incentives to fulfil its multiple roles? How does the FMI ensure that this is the case?*

The Depository's senior management has to be of sufficiently good repute and experience so as to ensure the sound and prudent management of the Depository. The management body shall be composed of suitable members of sufficiently good repute with an appropriate mix of skills, experience and knowledge of the entity and of the market (*Article 27(1) and (4) of the CSDR*). Only a person, who meets the fit and proper test requirements provided in the CSDR RTS, has the education, experience and professional qualifications necessary to perform his or her duties and who has an impeccable business reputation may become a member of the Supervisory Council or the Management Board of the Depository.

If a member of the Management Board or the Supervisory Council does not meet the requirements of the CSDR, the competent body of the Depository has to immediately revoke the respective member on its own initiative or upon the request of the FCMC.

Q.2.4.2: *What incentives does the FMI provide to board members so that it can attract and retain members of the board with appropriate skills? How do these incentives reflect the long-term achievement of the FMI's objectives?*

Members of the Depository's the Management Board are subject to Nasdaq target setting and performance evaluation and appraisal system which provides well documented procedures to review the performance of each member of the Management Board. This includes Employee Share Purchase programme and restricted stock program with long-term vesting schedule to facilitate achievement of the Depository's objectives in long-term.

Q.2.4.3: *Does the board include non-executive or independent board members? If so, how many?*

The Supervisory Council of the Depository includes 2 independent members in compliance with Article 27(2) of the CSDR.

Q.2.4.4: *If the board includes independent board members, how does the FMI define an independent board member? Does the FMI disclose which board member(s) it regards as independent?*

Independent member of Supervisory Council must not be an officer or employee of the Depository or its subsidiaries or any other individual having a relationship that, in the opinion of the Depository's Supervisory Council, would interfere with the exercise of independent judgment in carrying out the responsibilities of a member of Supervisory Council. The information on the structure of Supervisory Council (including the identification of independent members) shall be published in the official website of the Depository.

Key consideration 5: The roles and responsibilities of management should be clearly specified. An FMI's management should have the appropriate experience, a mix of skills, and the integrity necessary to discharge their responsibilities for the operation and risk management of the FMI.

Roles and responsibilities of management

Q.2.5.1: *What are the roles and responsibilities of management, and are they clearly specified?*

Please refer to information provided under Q.2.3.1 above.

Q.2.5.2: *How are the roles and objectives of management set and evaluated?*

These roles are set and evaluated on the basis of the size, complexity and nature of the Depository's operations that, among others, requires managerial capabilities and focus on risk management and IT arrangements.

Experience, skills and integrity

Q.2.5.3: *To what extent does the FMI's management have the appropriate experience, mix of skills and the integrity necessary for the operation and risk management of the FMI? How does the FMI ensure that this is the case?*

On the date of this self-assessment the Management Board of the CSD LV is composed of 3 individuals that are experienced and have proven expertise in the area of CSD services. The Supervisory Council of the CSD LV consists of 5 members (2 of which represent participants and issuers) that have proven expertise in the area of management of CSD services.

Please refer to information provided under Q. 2.4.1 above regarding the experience and skills of the management.

Q.2.5.4: *What is the process to remove management if necessary?*

Member of the Supervisory Council may be revoked at any time by a decision of the shareholders meeting (*Article 296(7) of Latvian Commercial Law*).

Member of the Management Board may be revoked by the decision of the Supervisory Council due to an important reason (*Article 306(1) of Latvian Commercial Law*). Furthermore, if a member of the Management Board or the Supervisory Council does not meet the requirements of the CSDR, the competent body has to immediately revoke the respective member on its own initiative or upon the request of the FCMC.

Key consideration 6: The board should establish a clear, documented risk -management framework that includes the FMI's risk-tolerance policy, assigns responsibilities and accountability for risk decisions, and addresses decision making in crises and emergencies. Governance arrangements should ensure that the risk-management and internal control functions have sufficient authority, independence, resources, and access to the board.

Risk management framework

Q.2.6.1: *What is the risk management framework that has been established by the board? How is it documented?*

The Depository has robust governance arrangements, which include effective processes to identify, manage, monitor and report the risks to which it is or might be exposed in compliance with Article 26(1) of the CSDR. Furthermore, the Depository maintains a sound risk-management framework for comprehensively managing legal, business, operational and other direct or indirect risks, including measures to mitigate fraud and negligence in compliance with Article 42 of the CSDR.

The Depository's approach is based on Enterprise Risk Management (**ERM**) approach in alignment with the COSO ERM Framework. The Depository's risks management arrangements need to comply with Baltic Market Risk management framework which requires regular assessment of **all risks** in terms of probability and impact of any occurrence, as well as action plans to mitigate the risks. Comprehensive risk self-assessment is conducted at least annually under the coordination of Nasdaq Group Risk Management function.

The Depository is also subject to extensive governmental regulation and scrutiny in the field of data security and IT risk management. The Depository places focus on IT risks and separate layer of IT risk management which is partly outsourced to a designated service provider.

Nasdaq Group Internal audit carries out audits in accordance with the internal audit plan or, if needed, on *ad hoc* basis.

Q.2.6.2: *How does this framework address the FMI's risk tolerance policy, assign responsibilities and accountability for risk decisions (such as limits on risk exposures), and address decision-making in crises and emergencies?*

The Depository's framework provides comprehensive mapping of risks, their incidence and possible implications as well as provides an action plan for the elimination or reduction of any risk that exceeds the Depository's tolerance limit.

The Supervisory Council and the Management Board assumes final responsibility and accountability for managing the Depository's risks. The Supervisory Council defines and determines an appropriate level of risk tolerance, and risk bearing capacity for the Depository, for all the services the Depository provides, including Settlement Systems. The Management Board and the Supervisory Council ensure that the Depository's policies, procedures and controls are consistent with the Depository's risk tolerance and risk bearing capacity.

The Depository maintains a risk management function, compliance and internal control function and an audit function that is separate from other functions. The chief risk officer has to implement the risk management framework including policies and procedures established by the management bodies. The chief risk officer, the chief compliance officer and the internal control and audit function each have to have separate reporting line to the Management Board and direct access to the Supervisory Council in compliance with the CSDR RTS.

The Depository's business continuity and disaster recovery plan provides for measures and allocation of responsibilities in order to ensure continuity of the Depository's operations in emergencies and crisis situations.

Q.2.6.3: *What is the process for determining, endorsing and reviewing the risk management framework?*

Risk management framework and its suitability are under constant evaluation and monitoring of the Nasdaq Group Risk Management function, Baltic Risk Officer and Risk Coordinator. Changes in this framework will be notified and implemented according to the instructions of Nasdaq Group Risk Management, Baltic Risk Officer and local Risk Coordinator.

The Depository's risk management framework including policies and procedures is established by its Supervisory Council and implemented by the chief risk officer (see information provided under Q.2.6.2 above).

The Depository maintains an internal audit function which is separate from its other functions and activities and which has the following tasks:

- (i) to establish and implement and maintain an audit plan (reviewed and reported to FCMC at least on an annual basis) to examine and evaluate the adequacy and effectiveness of the Depository's systems, internal control mechanisms and governance arrangements;
- (ii) issue and verify compliance with the recommendations based on the examination and evaluation performed by the audit function;
- (iii) to report internal audit matters to the Management Board and Supervisory Council.

The Depository's operations, risk management processes, internal control mechanisms. Including operational risk management framework and systems are subject to independent audit which is performed at least every two years.

The Depository regularly evaluates and, where necessary, adjusts the risk management framework.

Authority and independence of risk management and audit functions

Q.2.6.4: *What are the roles, responsibilities, authority, reporting lines and resources of the risk management and audit functions?*

Nasdaq Inc. Board of Directors has the overall responsibility for ensuring that an adequate and well-functioning process for risk management has been implemented throughout the group. The management (including Management Board and Supervisory Council or other similar collective bodies of management) of each legal entity have the fiduciary risk management duties relating to their respective legal entity. This also includes managing specific risk related issues as governed by local regulatory requirements or local market practices.

To support management bodies, a role of Risk Coordinator has been designed for each regulated legal entity within Nasdaq group. The Risk Coordinator of the Depository shall also fulfil the role of chief risk officer within the meaning of CSDR.

Risk Coordinator has a direct reporting line to the Management Board of the Depository and direct access to the Supervisory Council of the Depository.

The main duties of the Risk Coordinator in relation to the Depository are:

- (i) to provide assurance to the management bodies that the Depository is compliant with legal and regulatory requirements in the area of risk management;
- (ii) to provide support to the management in related regulatory issues;
- (iii) to facilitate any coordination efforts that may be required for the legal entity to exercise control over its own risk environment;
- (iv) to provide assurance that appropriate plans and procedures, specific to the legal entity, has been developed and are properly maintained and tested;
- (v) to maintain documentation, specific to the legal entity, in an assigned repository shared with other members within the network of Risk Officers and Coordinators of Nasdaq Group;
- (vi) to liaise with Risk Officers within the business line organization, to ensure that the legal perspective is being addressed and that the legal entity is able to operate accordingly.

Global Risk Management is responsible for providing information, training, support and guidance to the Risk Coordinators in fulfilling their roles.

Risk Coordinator shall cooperate closely with Baltic Risk Officer who has overall duty for Risk control arrangements within the legal entities belonging to Baltic Market, including:

- Facilitate the implementation and understanding of Group risk management policies & directives;
- Manage risk assessments being conducted on at least an annual basis and risk insurance;
- Provide assurance that relevant Business Continuity Plans have been developed, are properly maintained and regularly tested.
- Maintain of up-to-date emergency response and Crisis management plans;
- Coordinate risk and incident reporting to the Business Unit Head and to Global Risk Management;
- Support business line management and Risk Coordinators within the legal entity structure.

Further, reports on litigations, operational incidents and compliance issues are presented to the Supervisory Council of the Depository at each ordinary meeting.

Nasdaq Group Internal audit carries out audits in accordance with the internal audit plan or on ad hoc basis if needed.

Q.2.6.5: *How does the board ensure that there is adequate governance surrounding the adoption and use of risk management models? How are these models and the related methodologies validated?*

Risk management framework and its suitability are under constant evaluation and monitoring of the Nasdaq Group Risk Management function, Baltic Risk Officer and Risk Coordinator (i.e. chief risk officer of the Depository). Changes to this framework are notified and implemented according to the instructions of Nasdaq Group Risk Management, Baltic Risk Officer and local Risk Coordinator.

Key consideration 7: The board should ensure that the FMI's design, rules, overall strategy, and major decisions reflect appropriately the legitimate interests of its direct and indirect participants and other relevant stakeholders. Major decisions should be clearly disclosed to relevant stakeholders and, where there is a broad market impact, the public.

Identification and consideration of stakeholder interests

Q.2.7.1: *How does the FMI identify and take account of the interests of the FMI's participants and other relevant stakeholders in its decision-making in relation to its design, rules, overall strategy and major decisions?*

The Depository engages its participants continuously through the following forums in order to understand their needs, expectations and take into account their legitimate interests:

- (i) User Committee for each Settlement System. See information provided under Q. 2.2.1 above regarding the competency of the User Committee;
- (ii) participant round tables (at least twice a year);
- (iii) *ad hoc* consultations launched in the event of important projects (such as replacement of the CSD system) or special purpose meetings;
- (iv) special purpose joint working groups (e.g. T2S national user group);
- (v) mandatory advance notice about any changes to the Depository's rules.

As a matter of general practice, CSD LV, CSD EE and CSD LT have consulted with participants, its supervisor and overseer prior to every major strategic decision that could have material implications for the local market.

Q.2.7.2: *How does the board consider the views of direct and indirect participants and other relevant stakeholders on these decisions; for example, are participants included on the risk management committee, on user committees such as a default management group or through a public consultation? How are conflicts of interest between stakeholders and the FMI identified, and how are they addressed?*

Consideration of the view of the participants

User Committee has a right to submit a non-binding opinion to the Management Board of the Depository containing detailed reasons regarding the pricing structures of the Depository or any other issue which the User Committee considers important and having impact on its members (Article 28(4) of the CSDR and the Rules of Procedure of the User Committee for the respective Settlement System, hereinafter the "Rules of Procedure").

The User Committee reviews audit findings together with the Depository where:

- (i) such findings relate to the mandate of the User Committee, in particular on key arrangements that impact the users of the Depository, including criteria for accepting issuers or participants to the Settlement System;
- (ii) findings may impact the level of provision of services by the Depository, including ensuring business continuity (Article 28 of the CSDR and the Rules of Procedure).

Under Article 28(6) of the CSDR the Depository has to promptly inform the competent authority and the User Committee of any decision in which the management body decides not to follow the advice of the User Committee. The User Committee may inform the competent authority of any areas in which it considers that the advice of the User Committee has not been followed (see also the Rules of Procedure).

The Management Board may also request the User Committee to provide non-binding advice and/or opinion regarding any activities and/or decisions of the Depository. In such case the User Committee has to provide its advice and/or opinion to the Management Board within 30 business days following the receipt of the request (the Rules of Procedure).

For more information on the consultations with the stakeholders please refer to information provided under Q. 2.7.1 above.

Conflicts of interest

The conflicts of interest between the members of the User Committee and the Depository are identified and assessed in accordance with Section 7 of the Rules of Procedure which implements the CSDR RTS:

- (i) the advice or non-binding opinion of the User Committee are independent from any direct influence by the Depository, including the Management Board.
- (ii) each member has to disclose potential conflicts of interest in any matters discussed in the User Committee.
- (iii) where the chairman of the User Committee determines that the Member of the User Committee has an actual or potential conflict of interest on a particular matter that member shall not be allowed to vote on that matter.
- (iv) each time before disclosing audit finding to the User Committee, the Management Board takes into account potential conflicts of interest between the members of the User Committee and the Depository. In case the Management Board determines possible conflicts of interest between the members of the User Committee and the Depository, the Management Board has the right not to disclose audit findings to the User Committee.
- (v) representatives that are settlement internalisers are not to be provided with information that could place them in a competitive advantage or that otherwise may constitute a conflict of interests with the Depository.

Disclosure

Q.2.7.3: *To what extent does the FMI disclose major decisions made by the board to relevant stakeholders and, where appropriate, the public?*

The Depository discloses major decisions to the stakeholders and the public, as the minimum, to the extent that is necessary for the successful implementation of the decision. Please refer to information provided under Q.2.7.1 regarding consultations with the stakeholders (participants, issuers and competent authorities) regarding such issues as Depository's rules and tariffs.

Furthermore, the Depository communicates the results of the audits, where appropriate taking into account potential conflicts of interest between the members of the User Committee and the Depository, to the User Committee in accordance with Article 26(6) of the CSDR and CSDR RTS.

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Principle 3: Framework for the comprehensive management of risks

An FMI should have a sound risk-management framework for comprehensively managing legal, credit, liquidity, operational, and other risks.

In reviewing this principle, an assessor should consider how the various risks, both borne by and posed by the FMI, relate to and interact with each other. As such, this principle should be reviewed holistically with the other principles.

Key consideration 1: An FMI should have risk-management policies, procedures, and systems that enable it to identify, measure, monitor, and manage the range of risks that arise in or are borne by the FMI. Risk-management frameworks should be subject to periodic review.

Risks that arise in or are borne by the FMI

Q.3.1.1: *What types of risk arise in or are borne by the FMI?*

The Depository is exposed to risk categories and types that are universal to any financial infrastructure company: main risk categories being strategic, operational and commercial risks; and main risk types being environmental, delivery risks, process risks, human error, legal, technology, project risks, hazard risks and crime.

Q.3.1.2: *What are the FMI's policies, procedures and controls to help identify, measure, monitor and manage the risks that arise in or are borne by the FMI?*

Depository's policies, procedures and controls in the area of risk management are broadly based on Enterprise Risk Management (ERM) framework.

That among others includes regular assessment of all risks in terms of probability and impact of any occurrence, as well as action plans to mitigate the risks. Comprehensive risk self-assessment is conducted at least annually under the coordination of Nasdaq Group Risk Management function.

The Depository is the part of Nasdaq group where high standards and measures related to risk control are implemented. The primary responsibility for managing risks is aligned with the line management structure within Nasdaq group. Managers at all levels are responsible for the efficient implementation and execution of risk management within their own area of operational responsibility.

Further please refer to information provided under Q.2.6.4 above.

Q.3.1.3: *What risk management systems are used by the FMI to help identify measure, monitor and manage its range of risks?*

In addition to general ERM approach Depository uses Nasdaq B Wise GRC solution that offers role-based solutions which are seamlessly integrated for the needs of following functions of the Nasdaq group as whole:

- (i) Internal Audit
- (ii) Risk Management

- (iii) Compliance & Policy Management
- (iv) Internal Control
- (v) Information Security
- (vi) Sustainability Performance Management.

See <http://www.bwise.com/solutions> for additional information..

Q.3.1.4: *How do these systems provide the capacity to aggregate exposures across the FMI and, where appropriate, other relevant parties, such as the FMI's participants and their customers?*

Mapping and quantifying risks per regular risk self assessment supports aggregate exposures to be identified. Please see "Risk Self Assessment. Practical Guidelines on how to identify, assess and report risks" (available for Central Banks only) for more details about the methodology of risk identification and quantification.

Review of risk management policies, procedures and systems

Q.3.1.5: *What is the process for developing, approving and maintaining risk management policies, procedures and systems?*

Risk management framework and its suitability are under constant evaluation and monitoring of the Nasdaq Group Risk Management function, Baltic Risk Officer and Risk Coordinator of the Depository (Chief Risk Officer of the Depository). Changes in this framework will be notified and implemented according to the instructions of Nasdaq Group Risk Management, Baltic Risk Officer and Risk Coordinator of the Depository.

Q.3.1.6: *How does the FMI assess the effectiveness of risk management policies, procedures and systems?*

Risk management framework and its suitability (*including effectiveness of risk management policies, procedures and systems*) are under constant evaluation and monitoring of the Nasdaq Group Risk Management function, Baltic Risk Officer and Risk Coordinator. Changes in this framework will be notified and implemented according to the instructions of Nasdaq Group Risk Management, Baltic Risk Officer and Risk Coordinator of the Depository. Analysis of incidents (IT, operational or human error) will be important tool upon which to consider if any changes in the risk policies, procedures or systems have to be introduced.

Q.3.1.7: *How frequently are the risk management policies, procedures and systems reviewed and updated by the FMI? How do these reviews take into account fluctuation in risk intensity, changing environments and market practices?*

Risk management framework and its suitability (*including effectiveness of risk management policies, procedures and systems*) is subject to reviewed at least once per year, considering among others actual register of incidents or other similar loss generating events, errors or omissions.

Key consideration 2: An FMI should provide incentives to participants and, where relevant, their customers to manage and contain the risks they pose to the FMI.

Q.3.2.1: *What information does the FMI provide to its participants and, where relevant, their customers to enable them to manage and contain the risks they pose to the FMI?*

The Depository as any typical FMI shall disclose most of the information that is relevant in the context of risks management on its website. These include rules, market practice guides, various questionnaires and disclosures (including those required by the CSDR).

Further, the Rules requires that every Depository's participant has to maintain among others risk-management expertise, compliance, operational and technical arrangements that are adequate to prevent the occurrence of risk for the investors, Depository, other participants and the issuers.

Q.3.2.2: *What incentives does the FMI provide for participants and, where relevant, their customers to monitor and manage the risks they pose to the FMI?*

Risk profile of the Depository's operational model does not expose it to credit or financial risks generated by the participants.

Failed settlement is one of the risks that participants face from each other. There are discipline measures in place that penalise the failing participant for the failure of timely settlement. In the future these measures will be replaced by CSDR RTS on settlement discipline.

As regards operational, crime and other types of risks, then these need to be insured by the participants in cases where applicable law so provides.

Q.3.2.3: *How does the FMI design its policies and systems so that they are effective in allowing their participants and, where relevant, their customers to manage and contain their risks?*

In the context of Depository's operations it is mainly about the modern CSD System that enables participants to monitor their transactions throughout the full life cycle. IT tools, functions and services as mandated by the CSDR and T2S eforce and facilitate this direction even further.

Key consideration 3: An FMI should regularly review the material risks it bears from and poses to other entities (such as other FMIs, settlement banks, liquidity providers, and service providers) as a result of interdependencies and develop appropriate risk-management tools to address these risks.

Material risks

Q.3.3.1: *How does the FMI identify the material risks that it bears from and poses to other entities as a result of interdependencies? What material risks has the FMI identified?*

Please refer to the risk framework description under Q. 3.1.1 and 3.1.2. Nature of Depository's operations is such that IT and operational risks matter mostly as material risks in the context of interdependencies.

Q.3.3.2: *How are these risks measured and monitored? How frequently does the FMI review these risks?*

Please refer to information provided under Q. 3.1.4. The risks reviewed is completed at least annually.

Risk management tools

Q.3.3.3: *What risk management tools are used by the FMI to address the risks arising from interdependencies with other entities?*

These tools include among others:

- (i) Proper risk management framework;
- (ii) Proper IT security framework;
- (iii) Well designed business continuity policies and procedures;
- (iv) The failover, recovery and resuming of operations in a secondary processing site.

Q.3.3.4: *How does the FMI assess the effectiveness of these risk management tools? How does the FMI review the risk management tools it uses to address these risks? How frequently is this review conducted?*

Risk management framework, including tools listed under Q.3.3.3, and their suitability (*including effectiveness of risk management policies, procedures and systems*) are under constant evaluation and monitoring of the Nasdaq Group Risk Management function, Baltic Risk Officer and Risk Coordinator. Changes in this framework will be notified and implemented according to the instructions of Nasdaq Group Risk Management, Baltic Risk Officer and Risk Coordinator of the Depository. Business continuity policies and procedures are subject to regular tests on annual basis as a minimum.

Key consideration 4: An FMI should identify scenarios that may potentially prevent it from being able to provide its critical operations and services as a going concern and assess the effectiveness of a full range of options for recovery or orderly wind-down. An FMI should prepare appropriate plans for its recovery or orderly wind-down based on the results of that assessment. Where applicable, an FMI should also provide relevant authorities with the information needed for purposes of resolution planning.

Scenarios that may prevent an FMI from providing critical operations and services

Q.3.4.1: *How does the FMI identify scenarios that may potentially prevent the FMI from providing its critical operations and services? What scenarios have been identified as a result of these processes?*

Scenarios are identified as routine part of risk assessment framework. Following scenarios have been identified so far:

- (i) Revocation of a license;
- (ii) A claim for damages that would be payable by the Depository and that would exceed Depository's insurance limit and own capital and result in Depository's bankruptcy;
- (iii) Catastrophic event (nuclear explosion, asteroid impact) rendering operation of the Depository in the territory of the Latvia, Estonia or Lithuania impossible;
- (iv) Other circumstances where there is a lack of sufficient liquid resources for continuing Depository's operations.

Q.3.4.2: *How do these scenarios take into account both independent and related risks to which the FMI is exposed?*

These scenarios take into account both independent and related risks to the best of our understanding.

Recovery or orderly wind-down plans

Q.3.4.3: What plans does the FMI have for its recovery or orderly wind-down?

More specific recovery and wind-down plan, including its review policy, is work in progress pending for completion in January 2017. Reason being that many key components such as RTS under the CSDR and Report on the Recovery of financial market infrastructures by CPSS-IOSCO - potentially affecting the plan, have not been finalised yet.*

* See: <http://www.bis.org/press/p130812.htm> CPSS-IOSCO has published consultative report on the Recovery of financial market infrastructures.

Plan is likely to foresee that the Depository shall first request for additional funding from its parent company / Nasdaq Inc in the case of scenarios (B) and (D). Should parent company refuse or be unable to contribute, the Depository needs to request its participants to contribute necessary funding. If participants refuse or fail to contribute, it will result in as orderly wind down of the Depository if possible.

Means accumulated for this purpose under the capitalization requirements of the CSDR can be used for that purpose.

Q.3.4.4: *How does the FMI's key recovery or orderly wind-down strategies enable the FMI to continue to provide critical operations and services?*

More specific recovery and wind-down plan, including its review policy, is work in progress pending for completion in January 2017.

Q.3.4.5: *How are the plans for the FMI's recovery and orderly wind-down reviewed and updated? How frequently are the plans reviewed and updated?*

More specific recovery and wind-down plan, including its review policy, is work in progress pending for completion in 2017.

PS	CSD	SSS	CCP	TR
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<p>Principle 4: Credit risk</p> <p>An FMI should effectively measure, monitor, and manage its credit exposure to participants and those arising from its payment, clearing, and settlement processes. An FMI should maintain sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence. In addition, a CCP that is involved in activities with a more-complex risk profile or that is systemically important in multiple jurisdictions should maintain additional financial resources sufficient to cover a wide range of potential stress scenarios that should include, but not be limited to, the default of the two largest participants and their affiliates that would potentially cause the largest aggregate credit exposures to the CCP in extreme but plausible market conditions. All other CCPs should maintain, at a minimum, total financial resources sufficient to cover the default of the one participant and its affiliates that would potentially cause the largest aggregate credit exposures to the CCP in extreme but plausible market conditions.</p>

Because of the extensive interactions between the financial risk management and financial resources principles, this principle should be reviewed in the context of Principle 5 on collateral, Principle 6 on margin and Principle 7 on liquidity risk, as appropriate. This principle should also be reviewed in the context of Principle 13 on participant default rules and procedures, Principle 23 on disclosure of rules, key procedures and market data, and other principles, as appropriate.

The following key consideration applies to	PS	CSD	SSS	CCP	TR
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Key consideration 1: An FMI should establish a robust framework to manage its credit exposures to its participants and the credit risks arising from its payment, clearing, and settlement processes. Credit exposure may arise from current exposures, potential future exposures, or both.

Q.4.1.1: *What is the FMI's framework for managing credit exposures, including current and potential future exposures, to its participants and arising from its payment, clearing and settlement processes?*

The Depository does not operate as a licensed bank or CCP and does not provide banking type ancillary services within the meaning of the CSDR. The fundamental principle of the Depository as an operator of

the Settlement Systems is that it does not guarantee the transfer of funds nor securities and, hence, does not take credit risk related to such activities.

The framework for managing credit exposures, including current and potential future exposures to the Depository's participants is provided in the following.

1. Statutory basis

In Estonia, according to section (2) of § 272 of the SMA the registrar of the Estonian Central Register of Securities, while it is operating as an operator of a securities settlement system, does not have the right to guarantee the performance of claims and obligations arising on the basis of transfer orders or to assume other additional financial risks.

In Latvia and Lithuania, the law does not prevent the Depository from assuming credit risk. However, the Depository does not intend to provide in these countries services entailing credit risk or liquidity risk.

2. Rules

Under the Rules the Participant takes all the necessary measures to ensure smooth and timely settlement of every securities transaction on the ISD. The Participant shall send the instructions to the Settlement System only if the securities to be delivered or the cash balance due are available in the relevant account.

3. Authorisation under CSDR

The Depository intends to obtain an authorisation under the CSDR to provide only core CSD services and non-banking-type ancillary services that do not entail credit risk or liquidity risk.

4. Design of the clearing and settlement process

- (i) The Depository does not act as a CCP nor does it guarantee the transfer of funds or securities. The Depository executes the settlement on the basis of irrevocable transfer instructions only if funds and securities are available, save for cases when central bank auto-collateralisation is available to Payment Banks in T2S.
- (ii) the moment of entry (SF I) and the moment of irrevocability (SF II) of transfer orders is the moment when the Depository has established (either within the framework of trade-by-trade processing or optimisation algorithm) that all pre-conditions needed for the successful settlement are present (including balance-check of securities and cash of the sell and buy side in case of DvP).
- (iii) No event, including insolvency of the "buying participant" can prevent settlement of transfer orders after the settlement of transfer order is final (SF III) in T2S or CSD System, as a case may be.
- (iv) The finality of the settlement (SF III) is achieved via debits and credits on respective accounts (securities accounts and cash settlement accounts of the participant).

Under this model the Depository does not assume any credit risk because the transfer orders are settled only on a condition that balances in the accounts are sufficient or, in case of cash shortage in DCA, the Payment Bank in T2S may access central bank auto-collateralisation facility to obtain intra-day credit for settlement purposes. Nevertheless, the Depository does not assume any credit risk in relation to such auto-collateralisation facility.

5. Design of its services related to distribution of corporate proceeds

The Depository makes payments of corporate proceeds to account holders only if the Issuer until the start of the Settlement Day has transferred sufficient funds to the cash account of the Depository to execute corporate actions *the Rules*).

The above ensures that the Depository does not assume credit exposure to its participants as a result of the settlement services offered to its participants.

Q.4.1.2: *How frequently is the framework reviewed to reflect the changing environment, market practices and new products?*

Payment, clearing and settlement processes are part of routine risk assessment per general risk management framework (*please refer to questions under Principle 3*). Main design of the framework is provided by the applicable law. Minor reviews and changes are made on "as needed" basis. Framework has been designed in order to ensure the compliance of the Depository with the CSDR, RTS (e.g. settlement discipline) and T2S Rules (e.g. DCAs, auto-collateralisation, and corporate actions on "flow").

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 2: An FMI should identify sources of credit risk, routinely measure and monitor credit exposures, and use appropriate risk-management tools to control these risks.

Q.4.2.1: *How does the FMI identify sources of credit risk? What are the sources of credit risk that the FMI has identified?*

The services provided by the Depository are limited to core CSD services and certain non-banking type ancillary services not entailing credit risk or liquidity risk. The Depository does not itself intend to provide banking type ancillary services or to lend securities to its participants. All business processes and procedures have been designed to respect this limitation.

Q.4.2.2: *How does the FMI measure and monitor credit exposures? How frequently does and how frequently can the FMI recalculate these exposures? How timely is the information?*

Please refer to information provided under Q. 4.2.1 above.

Q.4.2.3: *What tools does the FMI use to control identified sources of credit risk (for example, offering an RTGS or DvP settlement mechanism, limiting net debits or intraday credit, establishing concentration limits, or marking positions to market on a daily or intraday basis)? How does the FMI measure the effectiveness of these tools?*

The following tools are available to participants to control *participant-to-participant* credit risk:

- (i) automation on T2S Platform and CSD System;
- (ii) DvP settlement mechanism;
- (iii) real time gross settlement without netting of either securities or cash leg and continuous recurrent settlement schedule with semi-hourly optimisation batches during business hours with intraday finality;
- (iv) settlement discipline measures (e.g. penalties for failure deliver securities on ISD and reporting to competent authorities);
- (v) measures to address settlement fails (buy-in for securities leg and availability of central bank auto-collateralisation in T2S for cash leg); and
- (vi) participants' default management rules and processes.

The main tool offered by the Depository for participants is DvP settlement on T2S platform in recurring processing cycles throughout the day without netting of either securities or cash leg.

In the event of lack of securities or cash, the Depository, as a general rule, postpones the Settlement Day of the transactions that failed to settle as a result of last recurring settlement attempt of a given date and collects penalties on a daily basis for each settlement instruction that fails to settle on ISD until the transaction is settled or cancelled by the parties (and, following the entry into force of RTS on settlement discipline, applies and distributes such penalties to the participant suffering from the failed settlement). If the transaction is concluded on or registered with any Baltic Stock Exchange and delayed settlement endangers regular and reliable continuous operation of the regulated market, the Baltic Stock Exchange may:

- (i) use of guarantee fund of the respective Baltic Stock Exchange to cover lack of funds;
- (ii) replace the short principal (seller) with the member of the exchange, which mediated the trade.

The effectiveness of the tool is proven by the fact that no participant of the three Baltic CSDs so far has faced a single credit loss incident to (e.g. receipt of securities without the payment or *vice versa* payment of money without receiving securities) *per modus operandi* described herein.

In cases where the transaction is not concluded on or registered with the Baltic Stock Exchange or the Baltic Stock Exchange chooses not to apply default handling measures, the Depository may, following the entry into force of the RTS on settlement discipline, apply buy-in measures in accordance with such RTS.

The following key consideration applies to	PS •	CSD	SSS •	CCP	TR
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Key consideration 3: A payment system or SSS should cover its current and, where they exist, potential future exposures to each participant fully with a high degree of confidence using collateral and other equivalent financial resources (see Principle 5 on collateral). In the case of a DNS payment system or DNS SSS in which there is no settlement guarantee but where its participants face credit exposures arising from its payment, clearing, and settlement processes, such an FMI should maintain, at a minimum, sufficient resources to cover the exposures of the two participants and their affiliates that would create the largest aggregate credit exposure in the system.

Coverage of exposures to each participant

Q.4.3.1: *How does the payment system or SSS cover its current and, where they exist, potential future exposures to each participant? What is the composition of the FMI's financial resources used to cover these exposures? How accessible are these financial resources?*

The services provided by the Depository are limited to core CSD services and certain non-banking type ancillary services not entailing credit risk or liquidity risk. The Depository does not intend to provide banking type ancillary services or to lend securities to the participants. All business processes and procedures have been designed to respect this limitation. The Depository does not pre-finance cash leg or securities leg. This means that the Depository has no current or potential future exposure to its participants.

Under Article 47 of the CSDR the Depository has to maintain capital, retained earnings and reserves that are proportional to the risks stemming from the activities of the CSD. It shall be at all times sufficient to:

- (i) ensure that the Depository is adequately protected against operational, legal, custody, investment and business risks so that the Depository can continue to provide services as a going concern;

- (ii) ensure an orderly winding-down or restructuring of the Depository's activities over an appropriate time span of at least six months under a range of stress scenarios.

The capital, earnings and reserves should be sufficient to absorb potential losses arising from the Depository's activities. The Depository does not have other special-purpose financial resources.

Furthermore, under Article 22(2) of the CSDR the Depository will be under the requirement to submit to the competent authority an adequate recovery plan to ensure continuity of its critical operations.

Please refer to information provided under Q.4.2.3 above regarding managing of participant-to-participant exposure.

With respect to **Latvian Settlement System**, please refer to information provided under Q.7.6.2 below regarding holding and management of corporate action proceeds accrued by the shareholders registered in the Initial Register.

Q.4.3.2: *To what extent do these financial resources cover the payment system's or SSS's current and potential future exposures fully with a high degree of confidence? How frequently does the payment system or SSS evaluate the sufficiency of these financial resources?*

Not applicable. However, it is worth mentioning that the operators of Baltic Stock Exchanges maintain a guarantee fund that is recalculated semi-annually taking into account the member's trading activity during the last 6 months. The minimum contribution of the exchange member at all times is EUR 5,000. The Baltic Stock Exchange operator may also request extraordinary contributions. The grounds, amount of and the procedure of payment thereof are determined upon an individual decision of the Baltic Stock Exchange operator, taking into account the increase in trading activity or other relevant circumstances that have been indicative of the necessity to increase the amount of the guarantee fund.

For DNS payment systems and DNS SSSs in which there is no settlement guarantee

Q.4.3.3: *If the payment system or SSS is a DNS system in which there is no settlement guarantee, do its participants face credit exposures arising from the payment, clearing and settlement processes? If there are credit exposures in the system, how does the system monitor and measure these exposures?*

Not applicable since none of its Settlement Systems is a DNS SSS.

Q.4.3.4: *If the payment system or SSS is a DNS system in which there is no settlement guarantee and has credit exposures among its participants, to what extent does the payment system's or SSS's financial resources cover, at a minimum, the default of the two participants and their affiliates that would create the largest aggregate credit exposure in the system?*

Not applicable.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 7: An FMI should establish explicit rules and procedures that address fully any credit losses it may face as a result of any individual or combined default among its participants with respect to any of their obligations to the FMI. These rules and procedures should address how potentially uncovered credit losses would be allocated, including the repayment of any funds an FMI may borrow from liquidity providers. These rules and procedures should also indicate the

FMI's process to replenish any financial resources that the FMI may employ during a stress event, so that the FMI can continue to operate in a safe and sound manner.

Allocation of credit losses

Q.4.7.1: *How do the FMI's rules and procedures explicitly address any credit losses it may face as a result of any individual or combined default among its participants with respect to any of their obligations to the FMI? How do the FMI's rules and procedures address the allocation of uncovered credit losses and in what order, including the repayment of any funds an FMI may borrow from liquidity providers?*

Not applicable (please refer to information provided under Q.4.1.1 above).

Replenishment of financial resources

Q.4.7.2: *What are the FMI's rules and procedures on the replenishment of the financial resources that are exhausted during a stress event?*

Not applicable (please refer to information provided under Q.4.1.1 above).

PS	CSD	SSS	CCP	TR
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Principle 7: Liquidity risk

An FMI should effectively measure, monitor, and manage its liquidity risk. An FMI should maintain sufficient liquid resources in all relevant currencies to effect same-day and, where appropriate, intraday and multiday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of the participant and its affiliates that would generate the largest aggregate liquidity obligation for the FMI in extreme but plausible market conditions.

Because of the extensive interactions between the financial risk management and financial resources principles, this principle should be reviewed in the context of Principle 4 on credit risk, Principle 5 on collateral and Principle 6 on margin, as appropriate. This principle should also be reviewed in the context of Principle 8 on settlement finality, Principle 13 on participant default rules and procedures, Principle 23 on disclosure of rules, key procedures and market data, and other principles, as appropriate.

The following key consideration applies to	PS	CSD	SSS	CCP	TR
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Key consideration 1: An FMI should have a robust framework to manage its liquidity risks from its participants, settlement banks, nostro agents, custodian banks, liquidity providers, and other entities.

Q.7.1.1: *What is the FMI's framework for managing its liquidity risks, in all relevant currencies, from its participants, settlement banks, nostro agents, custodian banks, liquidity providers and other entities?*

The Depository does not operate as a licensed bank or CCP and does not itself provide banking type ancillary services within the meaning of the CSDR. The fundamental principle of the Depository as an operator of the Settlement Systems is that it does not guarantee the transfer of funds nor securities (see also 4.1.1 above).

Settlement is commenced on the condition that all pre-conditions for successful settlement are satisfied, including balance-check of securities and cash of the sell and buy side. Transfer orders after they have become irrevocable in T2S (T2S eligible securities) or CSD System (non-T2S eligible securities) cannot be withdrawn or amended. The transfer of funds under DvP transfer orders is final when the settlement amount is debited from the cash account of delivering Participant and credited to the cash account of the receiving Participant. Transfers cannot be unwound.

Q.7.1.2: *What are the nature and size of the FMI's liquidity needs, and the associated sources of liquidity risks, that arise in the FMI in all relevant currencies?*

At the moment the Depository's authorisation to provide CSD services under the CSDR will become effective it will offer settlement only in euro. The cash leg of securities transfers is settled via cash accounts in the respective T2 Component System according to the autonomous central bank model. Please refer to answers under Q.7.1.1 and Q.5.1.1 above.

In order to provide cash leg settlement in commercial bank money in other currencies (i.e. through accounts opened with a credit institution) CSD either needs to:

- become authorized as a credit institution; or
- designate one or more credit institutions meeting the requirements under Article 54 (4) of the CSDR if such cash settlement exceeds one per cent of the total value of all securities transactions against cash settled in the books of the Depository.

Depository has no intention to become authorized as a credit institution. Thus it is important to note that services requiring the settlement of cash leg in non-EUR currencies in commercial bank money likely to exceed 1% threshold shall be available if and only if credit institution(s) meeting the requirements of Article 54 (4) of the CSDR can be designated by Depository based on reasonable commercial terms.

Q.7.1.3: *How does the FMI take into account the potential aggregate liquidity risk presented by an individual entity and its affiliates that may play multiples roles with respect to the FMI?*

The Depository's settlement model is designed to function so that it is remarkably immune to liquidity risks (participant to participant and participant to system operator). The Participants may access central bank auto-collateralisation in T2S in order to obtain intraday credit to cover any shortage of funds in the DCAs. Participants can manage and monitor their liquidity and related risks via convenient interface of CSD System and by priority levels assigned to transfer orders.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 2: An FMI should have effective operational and analytical tools to identify, measure, and monitor its settlement and funding flows on an on-going and timely basis, including its use of intraday liquidity.

Q.7.2.1: *What operational and analytical tools does the FMI have to identify measure and monitor settlement and funding flows?*

The Depository provides a convenient interface to Participants for monitoring the settlement and funding flows in T2S and CSD System. There is a specific browser for monitoring of cash positions that provides information on the currently available funds, funds needed for the settlement of pending transfers of the current day, settled positions and cash forecast.

The Cash Agent and in some cases the settlement parties may obtain the cash forecast in GUI and via messaging from CSD System which includes the information on net total of accepted pending settlement instructions (CSD System and T2S), cash balance of the CSA in CSD System and expected cash balance.

The Payment Bank in T2S may request from T2S via CSD System's GUI current settlement day cash information report (information for transactions pending to settle during the current Settlement Day) and following settlement day cash forecast report (information for the next settlement day considering the instructions that are expected to be settled the following Settlement Day).

Q.7.2.2: *How does the FMI use those tools to identify measure and monitor its settlement and funding flows on an on-going and timely basis, including its use of intraday liquidity?*

The settlement and funding flows are monitored continuously on a daily basis. Cash Agents through cash forecasts and CSD System's GUI can monitor the net settlement amounts of the Account Operators to which they provide liquidity services. The Depository maintains an up-to-date contact list of Participants which may be used in case of default situations.

The following key consideration applies to	PS •	CSD	SSS •	CCP	TR
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Key consideration 3: A payment system or SSS, including one employing a DNS mechanism, should maintain sufficient liquid resources in all relevant currencies to effect same-day settlement, and where appropriate intraday or multiday settlement, of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of the participant and its affiliates that would generate the largest aggregate payment obligation in extreme but plausible market conditions.

Q.7.3.1: *How does the payment system or SSS determine the amount of liquid resources in all relevant currencies to effect same day settlement and, where appropriate, intraday or multiday settlement of payment obligations? What potential stress scenarios (including, but not limited to, the default of the participant and its affiliates that would generate the largest aggregate payment obligation in extreme but plausible market conditions) does the payment system or SSS use to make this determination?*

The Depository requires Participants to pre-finance cash leg of their outstanding buy side DvP transfer orders before it initiates the settlement processing of the given transfer orders. Before the settlement starts on the ISD the Cash Agent has to transfer sufficient funds to its DCA, the Depository's account in T2 Component System or the cash account opened in Clearstream LUX. The Depository provides cash forecast to participants based on the total value of such transfer orders (see 7.2.1 above).

Under Article 41(3) of the CSDR the Depository is under an obligation to undertake with its participants and other relevant stakeholders periodic testing and review of its default procedures to ensure that they are practical and effective.

Q.7.3.2: *What is the estimated size of the liquidity shortfall in each currency that the payment system or SSS would need to cover?*

Not applicable since the Depository and its Settlement Systems is not going to cover liquidity shortfalls. Please refer to the answer under Q. 7.3.1.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 5: For the purpose of meeting its minimum liquid resource requirement, an FMI's qualifying liquid resources in each currency include cash at the central bank of issue and at creditworthy commercial banks, committed lines of credit, committed foreign exchange swaps, and committed repos, as well as highly marketable collateral held in custody and investments that are readily available and convertible into cash with prearranged and highly reliable funding arrangements, even in extreme but plausible market conditions. If an FMI has access to routine credit at the central bank of issue, the FMI may count such access as part of the minimum requirement to the extent it has collateral that is eligible for pledging to (or for conducting other appropriate forms of transactions with) the relevant central bank. All such resources should be available when needed.

Size and composition of qualifying liquid resources

Q.7.5.1: *What is the size and composition of the FMI's qualifying liquid resources in each currency that is held by the FMI? In what manner and within what time frame can these liquid resources be made available to the FMI?*

Not applicable. Please refer to response under Q.7.3.1. and 7.3.2.

Availability and coverage of qualifying liquid resources

Q.7.5.2: *What prearranged funding arrangements has the FMI established to convert its readily available collateral and investments into cash? How has the FMI established that these arrangements would be highly reliable in extreme but plausible market conditions? Has the FMI identified any potential barriers to accessing its liquid resources?*

Not applicable to the Depository since the Depository does not accept collateral, offers cash settlement services only in CeBM and only euro and, as a general rule, does not hold assets that require conversion into cash.

As regards the **Latvian Settlement System**, the Depository may invest the accrued corporate action proceeds by the shareholders registered in the Initial Register and held in safe custody by the Depository only in highly liquid low risk debt securities that can be easily converted into cash in order to distribute such proceeds to the shareholders (*the Financial Instruments Market Law*).

Q.7.5.3: *If the FMI has access to routine credit at the central bank of issue, what is the FMI's relevant borrowing capacity for meeting its minimum liquid resource requirement in that currency?*

The Depository does not have access to routine credit at the central bank in order to guarantee securities transaction settlement.

Q.7.5.4: *To what extent do the size and the availability of the FMI's qualifying liquid resources cover its identified minimum liquidity resource requirement in each currency to effect settlement of payment obligations on time?*

Size of qualifying resources (only in €) is determined by the amounts that participants have pre-financed to the Payment Bank's DCA in T2S or the Depository's RTGS account in T2 Component System. It varies and depends on the total amount of outstanding (unsettled) DvP buy side transfer orders for the given settlement date. Failure to pre-finance Depository's account in T2S Component System means that some or all of given participant's buy side transfer orders may fail to settle unless liquidity generated by sell side transfer orders covers the liquidity shortfall or central bank intraday credit is available through auto-collateralisation facility in T2S.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 6: An FMI may supplement its qualifying liquid resources with other forms of liquid resources. If the FMI does so, then these liquid resources should be in the form of assets that are likely to be saleable or acceptable as collateral for lines of credit, swaps, or repos on an ad hoc basis following a default, even if this cannot be Reliably prearranged or guaranteed in extreme market conditions. Even if an FMI does not have access to routine central bank credit, it should still take account of what collateral is typically accepted by the relevant central bank, as such assets may be more likely to be liquid in stressed circumstances. An FMI should not assume the availability of emergency central bank credit as a part of its liquidity plan.

Size and composition of supplemental liquid resources

Q.7.6.1: *What is the size and composition of any supplemental liquid resources available to the FMI?*

The Depository does not guarantee settlement of securities or cash and, hence, does not maintain supplemental liquid resources.

Nasdaq Riga AS, Nasdaq Tallinn AS and Nasdaq Vilnius AB (hereinafter “Baltic Stock Exchanges”) maintain a guarantee fund that may be used in accordance with the Rules and Regulations of the respective Baltic Stock Exchange to facilitate the settlement of unsettled stock exchange transactions. Assets of the said guarantee fund are held in cash with the respective central bank. On the date of this self-assessment the amount of:

- (i) **Nasdaq Tallinn** guarantee fund was EUR 73 292;
- (ii) **Nasdaq Riga** guarantee fund was EUR 35 538;
- (iii) **Nasdaq Vilnius** guarantee fund was EUR 61 919.

Availability of supplemental liquid resources

Q.7.6.2: *How and on what basis has the FMI determined that these assets are likely to be saleable or acceptable as collateral to obtain the relevant currency, even if this cannot be reliably prearranged or guaranteed in extreme market conditions?*

Not applicable to the Depository. As regards Latvian Settlement System, please see answer under Q. 7.5.2 above regarding investment of corporate action proceeds accrued by the shareholders registered in the Initial Register.

Q.7.6.3: *What proportion of these supplemental assets qualifies as potential collateral at the relevant central bank?*

Not applicable.

Q.7.6.4: *In what circumstances would the FMI use its supplemental liquid resources in advance of, or in addition to, using its qualifying liquid resources?*

Not applicable.

Q.7.6.5: *To what extent does the size and availability of the FMI's supplemental liquid resources, in conjunction with its qualifying liquid resources, cover the relevant liquidity needs identified through the FMI's stress test programme for determining the adequacy of its liquidity resources (see key consideration 9)?*

The Depository does not guarantee settlement of securities or cash and, hence, does not maintain supplemental liquid resources. Size of qualifying resources (only in €) is determined by the amounts that participants have pre-financed to the Depository's T2 account (please see answer under Q. 7.5.1 above).

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 7: An FMI should obtain a high degree of confidence, through rigorous due diligence, that each provider of its minimum required qualifying liquid resources, whether a participant of the FMI or an external party, has sufficient information to understand and to manage its associated liquidity risks, and that it has the capacity to perform as required under its commitment. Where relevant to assessing a liquidity provider's performance reliability with respect to a particular currency, a liquidity provider's potential access to credit from the central bank of issue may be taken into account. An FMI should regularly test its procedures for accessing its liquid resources at a liquidity provider.

Use of liquidity providers

Q.7.7.1: *Does the FMI use a liquidity provider to meet its minimum required qualifying liquidity resources? Who are the FMI's liquidity providers? How and on what basis has the FMI determined that each of these liquidity providers has sufficient information to understand and to manage their associated liquidity risk in each relevant currency on an on-going basis, including in stressed conditions?*

The Depository requires participants to pre-finance cash leg of their outstanding buy side DvP transfer orders before the Depository initiates the settlement processing of transfer orders in question. The Account Operators have to ensure sufficient liquidity themselves or through a designated Cash Agent (for T2S eligible securities Payment Bank in T2S).

The Depository offers a convenient interface for monitoring the settlement and funding flows (liquidity needs). There is a specific browser for monitoring of cash positions that provides information on the currently available funds, funds needed for the settlement of pending transfers of the current day, settled positions and cash forecast. The Depository provides and determines cash forecast to participants based on the total value of such transfer orders (please see answer under Q .7.2.1 above).

Reliability of liquidity providers

Q.7.7.2: *How has the FMI determined that each of its liquidity providers has the capacity to perform on its commitment in each relevant currency on an on-going basis?*

The Depository determines capacity to perform on its commitment in euro through the participation requirements and monitoring tools. Only a credit institution licensed in the EU/EEA or third countries and authorised to provide credit institution's services in Estonia, Latvia or Lithuania are admitted to the Depository in the status of a Cash Agent.

Please refer to information provided under Q.7.7.1 above regarding the tools for monitoring the settlement and funding flows (liquidity needs).

Q.7.7.3: *How does the FMI take into account a liquidity provider's potential access to credit at the central bank of issue?*

Access to credit at the central bank is not a pre-condition to the membership or participant's operations.

Q.7.7.4: *How does the FMI regularly test the timeliness and reliability of its procedures for accessing its liquid resources at a liquidity provider?*

Not applicable to the Depository.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 8: An FMI with access to central bank accounts, payment services, or securities services should use these services, where practical, to enhance its management of liquidity risk.

Q.7.8.1: *To what extent does the FMI currently have, or is the FMI eligible to obtain, access to accounts, payment services and securities services at each relevant central bank that could be used to conduct its payments and settlements and to manage liquidity risks in each relevant currency?*

The settlement of the cash leg:

- (i) for **T2S eligible securities** in euro is performed via DCAs in CeBM;
- (ii) for **non-T2S eligible securities** in euro is performed via RTGS account in T2-Estonia, T2-Latvia or T2-Lithuania and CSA of the Cash Agent or the Depository in CSD System, as a case may be.

The Cash Agents have to transfer the cash necessary for settlement to DCAs in T2S or Depository's T2 account, which is mirrored to CSAs in CSD System. Settlement in CSD System is final after debiting and crediting CSAs of the Cash Agents (DvP transfer) or CSAs of the Depository and the Cash Agent (corporate action proceeds).

Q.7.8.2: *To what extent does the FMI use each of these services at each relevant central bank to conduct its payments and settlements and to manage liquidity risks in each relevant currency?*

The Depository will use these services to full extent. At the moment the Depository's authorisation to provide CSD services under the CSDR will become effective the Depository will offer cash settlement only in euro and only in CeBM (*see Principle 9 below*).

Q.7.8.3: *If the FMI employs services other than those provided by the relevant central banks, to what extent has the FMI analysed the potential to enhance the management of liquidity risk by expanding its use of central bank services?*

Not applicable.

Q.7.8.4: *What, if any, practical or other considerations to expanding its use of relevant central bank services have been identified by the FMI?*

At the moment the Depository's authorisation to provide CSD services under the CSDR will become effective the Depository will offer cash settlement only in CeBM.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 9: An FMI should determine the amount and regularly test the sufficiency of its liquid resources through rigorous stress testing. An FMI should have clear procedures to report the

results of its stress tests to appropriate decision makers at the FMI and to use these results to evaluate the adequacy of and adjust its liquidity risk-management framework. In conducting stress testing, an FMI should consider a wide range of relevant scenarios. Scenarios should include relevant peak historic price volatilities, shifts in other market factors such as price determinants and yield curves, multiple defaults over various time horizons, simultaneous pressures in funding and asset markets, and a spectrum of forward-looking stress scenarios in a variety of extreme but plausible market conditions. Scenarios should also take into account the design and operation of the FMI, include all entities that might pose material liquidity risks to the FMI (such as settlement banks, nostro agents, custodian banks, liquidity providers, and linked FMIs), and where appropriate, cover a multiday period. In all cases, an FMI should document its supporting rationale for, and should have appropriate governance arrangements relating to, the amount and form of total liquid resources it maintains.

Stress test programme

Q.7.9.1: *How does the FMI use stress testing to determine the amount and test the sufficiency of its liquid resources in each currency? How frequently does the FMI stress-test its liquid resources?*

Simulation of participant's failure to pre-finance the amount of its buy side transfer orders in € would lead to rejection (based on the check of settlement eligibility criteria) of respective buy side transfer orders until the elimination of liquidity gap.

Q.7.9.2: *What is the process for reporting on an on-going basis the results of the FMI's liquidity stress tests to appropriate decision-makers at the FMI, for the purpose of supporting their timely evaluation and adjustment of the size and composition of the FMI's liquidity resources and liquidity risk management framework?*

Outcome of tests will be shared without delay with the Management Board, chief risk officer, compliance and internal control function and to the Supervisory Council. In case of any relevant findings, outcome of the tests will also be shared with the relevant user committee.

Stress test scenarios

Q.7.9.3: *What scenarios are used in the stress tests, and to what extent do they take into account a combination of peak historic price volatilities, shifts in other market factors such as price determinants and yield curves, multiple defaults over various time horizons, simultaneous pressures in funding and asset markets, and a spectrum of forward-looking stress scenarios in a variety of extreme but plausible market conditions?*

Simulation of single or multiple participant's failure to pre-finance the amount of buy side transfer orders in € would simply lead to rejection (based on the check of settlement eligibility criteria) of respective buy side transfer orders until the elimination of liquidity gap.

Q.7.9.4: *To what extent do the scenarios and stress tests take into account the FMI's particular payment and settlement structure (for example, real-time gross or deferred net; with or without a settlement guarantee; DVP model 1, 2 or 3 for SSSs), and the liquidity risk that is borne directly by the FMI, by its participants, or both?*

Scenarios of stress tests will take into account every relevant aspect of the operational model of the Depository.

Q.7.9.5: *To what extent do the scenarios and stress tests take into account the nature and size of the liquidity needs, and the associated sources of liquidity risks, that arise in the FMI to*

settle its payment obligations on time, including the potential that individual entities and their affiliates may play multiples roles with respect to the FMI?

Scenarios of stress tests will take into account every relevant aspect of the operational model of the Depository.

Review and validation

Q.7.9.6: *How frequently does the FMI assess the effectiveness and appropriateness of stress test assumptions and parameters? How does the FMI's stress test programme take into account various conditions, such as a sudden and significant increase in position and price volatility, position concentration, change in market liquidity, and model risk including shift of parameters?*

The Depository assesses the effectiveness and appropriateness of its stress test assumptions and parameters at least once per year.

General stability of the financial sector, increased price volatility and market liquidity are of indirect relevance to the Depository's stress test programme.

Deteriorations in the above parameters are likely to result in higher rate of settlement failures which in turn may increase the likelihood that systematically failing Account Operators need to be subjected to suspension or termination proceedings pursuant to the CSDR and Rules (Default Rules in particular). That calls for increased readiness for prompt and proper application of Default Rules.

Q.7.9.7: *How does the FMI validate its risk management model? How frequently does it perform this validation?*

At least once per year.

Q.7.9.8: *Where and to what extent does the FMI document its supporting rationale for, and its governance arrangements relating to, the amount and form of its total liquid resources?*

Not relevant considering the Depository's operational model.

The following key consideration applies to	PS •	CSD	SSS •	CCP •	TR
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Key consideration 10: An FMI should establish explicit rules and procedures that enable the FMI to affect same-day and, where appropriate, intraday and multiday settlement of payment obligations on time following any individual or combined default among its participants. These rules and procedures should address unforeseen and potentially uncovered liquidity shortfalls and should aim to avoid unwinding, revoking, or delaying the same-day settlement of payment obligations. These rules and procedures should also indicate the FMI's process to replenish any liquidity resources it may employ during a stress event, so that it can continue to operate in a safe and sound manner.

Same day settlement

Q.7.10.1: *How do the FMI's rules and procedures enable it to settle payment obligations on time following any individual or combined default among its participants?*

The Depository uses CeBM for the settlement of cash leg of DvP transfer orders. The cash leg in euro is settled:

- (i) in case of **T2S eligible securities**, through a DCA of a Payment Bank linked to an operational account in T2S;
- (ii) in case of **non-T2S eligible securities**, through a cash account of a Cash Agent with T2 Component System and CSAs in CSD System.

The Participant meets its monetary obligations (i.e. cash leg calculated on the basis of outstanding settlement orders) by maintaining, transferring or obtaining sufficient cash position (liquidity) to the respective DCA in T2S or cash account in T2 Component System by a pre-defined deadline.

If securities transactions concluded on Baltic Stock Exchange are affected by liquidity shortfalls, they are removed from the settlement batch and are moved to RTGS on the same day until specific cut-off time to provide the failing participant with opportunity to generate the missing liquidity. In case the transaction is not settled on ISD, they are moved to next business day. If on ISD+3 liquidity is still not provided in the cash account, the guarantee fund of the Baltic Stock Exchange may be used to cover liquidity shortfall.

Q.7.10.2: *How do the FMI's rules and procedures address unforeseen and potentially uncovered liquidity shortfalls and avoid unwinding, revoking or delaying the same day settlement of payment obligations?*

The Depository's operating model (RTGS without settlement guarantee) makes unforeseen and potentially uncovered liquidity shortfalls, unwinding, revoking or delaying the same day settlement of payment obligations impossible.

Replenishment of liquidity resources

Q.7.10.3: *How do the FMI's rules and procedures allow for the replenishment of any liquidity resources employed during a stress event?*

Not applicable to the Depository and RTGS without settlement guarantee model.

Please refer to information provided under Q.4.3.2 above regarding replenishment of the guarantee fund of the operator of the Baltic Stock Exchange.

PS •	CSD	SSS •	CCP •	TR
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Principle 8: Settlement finality
An FMI should provide clear and certain final settlement, at a minimum by the end of the value date. Where necessary or preferable, an FMI should provide final settlement intraday or in real time.

In reviewing this principle, it should be noted that this principle is not intended to eliminate failures to deliver in securities trades. The occurrence of non-systemic amounts of such failures, although potentially undesirable, should not by itself be interpreted as a failure to satisfy this principle. This principle should be reviewed in the context of Principle 9 on money settlements, Principle 20 on FMI links, and other principles, as appropriate.

Key consideration 1: An FMI's rules and procedures should clearly define the point at which settlement is final.

Point of settlement finality

Q.8.1.1: *At what point is the settlement of a payment, transfer instruction or other obligation final, meaning irrevocable and unconditional? Is the point of settlement finality defined and documented? How and to whom is this information disclosed?*

General

The Depository outsources the validation, matching and settlement of all the Transfer Orders in T2S eligible securities (held in securities accounts that under the Rules migrate to T2S Platform) to T2S. The instructions concerning T2S eligible securities, settlement services and other T2S services are provided in an integrated technical T2S Platform. The Operational Accounts are reflected on T2S on one to one basis as T2S Securities Accounts. Only debits and credits of T2S eligible securities in T2S Securities Accounts create legal effects.

Non-T2S eligible securities are settled in CSD System, i.e. debits and credits of such securities in securities accounts in CSD System create legal effects.

The Depository operates the following Settlement Systems:

- (i) Estonian Settlement System which is governed by Estonian law;
- (ii) Latvian Settlement System which is governed by Latvian law;
- (iii) Lithuanian Settlement System which is governed by Lithuanian law.

The settlement finality is set out in the following rules:

- (i) T2S eligible securities are settled on T2S Platform according to the Rules, T2S Rules and T2S functionality;
- (ii) Non-T2S eligible securities are settled on CSD System according to the Rules and functionality of CSD System.

Any settlement finality moment (SF I, SF II or SF III) in the securities account is deemed to occur:

- (i) in case of T2S eligible securities, when T2S assigns a 'time stamp' in accordance with T2S Rules, regardless of whether the securities account records in CSD System have been synchronised with T2S data. After a settlement finality moment has occurred on T2S Platform, the records in the securities account with the respective Settlement System are continuously synchronised (at regular times and on ad hoc basis) with T2S records in accordance with T2S Rules and the user messaging subscription preferences; or
- (ii) in case of non-T2S eligible securities, when CSD assigns a 'time stamp' in its CSD System.

Settlement finality

Settlement finality in all the Settlement Systems operated by the Depository is subject to uniform rules. Sections 6.4 – 6.6 of Chapter I clearly define the settlement finality moments: moment of entry of Transfer Order (SF I), moment of irrevocability of Transfer Order (SF II) and moment of settlement finality (SF III). The Rulebook defines SF I and SF II in accordance with the Collective Agreement concluded between, among others, CSD EE, CSD LV and CSD LT and the Eurosystem.

Moment of entry (SF I)

Under section 6.4 of Chapter I of the Rules a Transfer Order is deemed entered into the Settlement System at the moment when Transfer Order has been validated with:

- (i) T2S technical rules by the T2S Platform - in the case of T2S eligible securities;
- (ii) technical rules of the CSD System - in the case of Non-T2S eligible securities.

Irrevocability (SF II)

Under Section 6.5 of Chapter I of the Rules a Transfer Order is irrevocable from the moment at which the Transfer Order is given a status "matched":

- (i) in the case of T2S eligible securities, on the T2S Platform, or
- (ii) in the case of non-T2S eligible securities, on CSD System.

The status "matched" means that the Transfer Order is or becomes incapable of being amended or cancelled in accordance with the respective T2S or CSD System procedures by a unilateral instruction of the Participant, or any third party, who wishes to have the order amended or deleted. If the Participant has entered in CSD System a technically matched Transfer Order, the Transfer Order is irrevocable only from the moment at which the Transfer Order is given a status "matched", in the case of T2S eligible securities, on T2S Platform, or, in case of non-T2S eligible securities, on CSD System.

A Participant or any third party, including without limitation any insolvency administrator of a Participant does not have a right to withdraw or revoke, or purport or attempt to withdraw or revoke, any Transfer Order from the time at which it becomes irrevocable. Any instruction for such revocation does not have any legal effect, and the Depository shall not process and disregard any such instruction.

Finality of settlement (SF III)

Under Section 6.6 of Chapter I of the Rules the settlement of securities transfer is final as from the moment at which T2S eligible securities are credited to the transferee's securities account on T2S Platform or non-T2S eligible securities are credited to the transferee's securities account on CSD System and, in case of DvP transfer, cash amount in relation to such securities transfer is credited to the transferor's cash account. As of this moment the transfer of securities to a securities account and, where applicable, transfer of cash to the cash account is **unconditional, irrevocable, irreversible and enforceable**.

Under Section 6.12. of Chapter I of the Rules settlement of cash transfers in Depository's cash account in T2 are reflected in CSD System by means of sub-bookkeeping records and these transfers are final when the settlement amount is debited from the CSA of the delivering Cash Agent's CSA (DvP transfer) or the Depository (corporate action proceeds) and credited to the receiving Cash Agent's CSA. This, however, does not prejudice the right of the Depository to apply contingency measures.

Q.8.1.2: *How does the FMI's legal framework and rules, including the applicable insolvency law(s), acknowledge the discharge of a payment, transfer instruction or other obligation between the FMI and its participants, or between participants?*

In addition to the provisions of the Rules described in answer to Q. 8.1.1 above, the following legal safeguards apply under the law applicable to the respective Settlement System implementing the Settlement Finality Directive in Estonia, Latvia and Lithuania.

Estonian Settlement System

Under § 224(1) of SMA a transfer order forwarded to the Depository in accordance with the system rules may not be withdrawn or amended as of the moment it has become irrevocable under the system rules (SF II). Acts performed after this moment with the aim of amending or cancelling a transfer order already made are void.

Under § 272(2) of the SMA transfer instructions entered into the system by the Participant (SF I) prior to opening of the insolvency proceedings shall be settled if that is possible considering the free balances on respective accounts on the basis of § 228 (2) of the SMA. The same shall apply to transfer orders submitted on the day of initiation of the insolvency proceedings provided that the Depository was not and did not have to be aware of the initiation of such proceedings. No settlement will be effected in case of insufficiency of balances.

Under § 228(3) of the SMA, if the transfer orders are forwarded to the Estonian Settlement System and executed in accordance with the Estonian Settlement System rules on the business day of the initiation of the insolvency proceedings of the System Participant, they shall be valid only if the Depository was neither aware, nor should have been aware, of the opening of such proceedings.

§ 9 of the ECSR Act stipulates that transfer of security (i.e. acquisition of rights applicable towards third parties) requires registration that includes also credit entry made by the Depository on the basis of a transfer order.

Latvian Settlement System

Under Article 10(1) of SFD LV nobody has a right to revoke the transfer order after it has become irrevocable according to the system rules (SF II).

Under Article 8(1) of SFD LV transfer orders and netting shall be legally enforceable and binding on third parties even in the event of insolvency proceedings opened against a participant, provided that transfer orders were entered into the system (SF I) before the moment of opening of such insolvency proceedings.

Under Article 8(2) of the SFD LV, if the transfer orders are entered into the system (SF I) after the moment of opening of insolvency proceedings and are executed within the business day, during which the opening of such proceedings occur, they shall be legally enforceable and binding on third parties only if, at the time that such transfer orders become irrevocable (SF II), the Depository was neither aware, nor should have been aware, of the opening of such proceedings.

Under Article 9(1) of SFD LV commencement of insolvency proceedings of a participant does not prevent to use the moneys in the settlement account or financial instruments in order to enable the participant to fulfil its obligation in the system or interoperable system it has on the business day of the commencement of insolvency proceedings.

Lithuanian Settlement System

Under Article 7(1) of the SFD LT transfer orders and netting shall be legally enforceable and binding on third parties even in the event of insolvency proceedings opened against a participant, provided that transfer orders were entered into the system (SFI) before the moment of opening of such insolvency proceedings.

Under Article 7(4) of SFD LT, if the transfer orders are entered into the system (SFI) after the moment when the operations of the system participant were suspended and/or bankruptcy proceedings were initiated against it and are executed within the business day, during which the suspension of operations and/or initiation of bankruptcy proceedings, they shall be valid and not disputed by third parties only if, after the time of settlement, the Depository can prove that it was neither aware, nor should have been aware, of the suspension of operations and/or the initiation of the bankruptcy proceedings.

Under Article 7(5) of SFD LT, if a transaction concluded prior to initiation of bankruptcy proceedings is recognised as invalid under Lithuanian law or the law regulating the bankruptcy of the system participant, or on other grounds, this shall not cancel transfer orders, payment instructions and their netting, and may affect the mutual rights and obligations of a payer and recipient, but not the system.

Under Article 7(6) of SFD LT a system participant and third parties may not revoke the transfer order and/or payment instruction after it has become irrevocable according to the Rules (SF II).

Q.8.1.3: *How does the FMI demonstrate that there is a high degree of legal certainty that finality will be achieved in all relevant jurisdictions (for example, by obtaining a well-reasoned legal opinion)?*

High degree of legal certainty that finality will be achieved in all relevant jurisdictions is based on the fact that all jurisdictions in which Depository operates have implemented SFD and they are subject to CSDR. All the relevant aspects of settlement finality of transfer orders in any Settlement System operated by the Depository as issuer CSD are determined in the Rules and the applicable law (Estonian law, Latvian law or Lithuanian law). Where the Depository acts as investor CSD, settlement finality in the securities settlement system of a foreign CSD is determined by the rules of relevant foreign CSD and the law applicable to such system (e.g. settlement finality in securities settlement system of Clearstream LUX acting in the capacity of issuer CSD is determined by its rules and the law of Luxembourg).

Further, the Depository reserves the right to request independent legal opinion to validate high degree of legal certainty in the cases with international or cross-border element(s): e.g. links, foreign issuers, and foreign participants.

Rules of foreign CSDs which have a CSD link arrangement with the Depository are publicly available.

Finality in the case of links

Q.8.1.4: *How does the FMI ensure settlement finality in the case of linkages with other FMIs?*

a) For an SSS, how is consistency of finality achieved between the SSS and, if relevant, the LVPS where the cash leg is settled?

The Depository is going to have the following links on the date of its migration to T2S:

- 1) Link with Clearstream Banking Luxembourg (CBL) where the Depository acts as an Investor CSD *via* its Latvian and Lithuanian Securities Settlement Systems;
- 2) Link with Polish Central Securities Depository (KDPW) where the Depository Acts as an Issuer CSD *via* its Estonian Securities Settlement System.

In case of link between the Depository and a foreign CSD, issuer CSD rules and procedures provide pre conditions for the settlement finality. Consistency is achieved *via* design of settlement processing that permits unconditional cross-border transfer only upon relevant confirmation of the issuer CSD. Issuer CSD provides relevant confirmation if and only if all preconditions (settlement of cash leg, sufficiency balances etc.) for settlement at the level of issuer CSD have been met.

In other words: the finality and irrevocability of settlement of Transfer Orders processed through link arrangement is established according to the timeframes and rules of the Issuer CSD. When the Depository acts as Investor CSD in connection with the link arrangement, it shall cancel Transfer Orders placed by its Participant upon Participant's request only if such cancellation does not violate the rules of the Issuer CSD.

b) For a CCP for cash products, what is the relation between the finality of obligations in the CCP and the finality of the settlement of the CCP claims and obligations in other systems, depending on the rules of the relevant CSD/SSS and payment system?

Not applicable.

Key consideration 2: An FMI should complete final settlement no later than the end of the value date, and preferably intraday or in real time, to reduce settlement risk. An LVPS or SSS should consider adopting RTGS or multiple-batch processing during the settlement day.

Final settlement on the value date

Q.8.2.1: *Is the FMI designed to complete final settlement on the value date (or same day settlement)? How does the FMI ensure that final settlement occurs no later than the end of the intended value date?*

Yes, the Depository provides both real-time gross settlement (RTGS) and continuous recurrent batch settlement during the business hours with intraday finality. The Depository ensures that final settlement occurs no later than the end of intended value date on condition that all preconditions for settlement (sufficiency of securities and cash, etc.) have been met before the last optimisation batch.

Q.8.2.2: *Has the FMI ever experienced deferral of final settlement to the next business day that was not contemplated by its rules, procedures or contracts? If so, under what circumstances? If deferral was a result of the FMI's actions, what steps have been taken to prevent a similar situation in the future?*

CSD system (namely its T2S release) will be a completely new system for the Depository which is why statements about the deferral can only be made in the future, after CSD System and Rules have been operational for some time.

Intraday or real-time final settlement

Q.8.2.3: *Does the FMI provide intraday or real-time final settlement? If so, how? How are participants informed of the final settlement?*

After migration to T2S the Depository will follow T2S business day for T2S eligible securities. T2S offers continuous securities settlement in two periods: night time settlement (NTS) and real-time gross settlement (RTGS). T2S settlement day schedule consist of five major periods:

- (i) Start of day (18:45 – 20:00);
- (ii) NTS (20:00 – 03:00);
- (iii) Maintenance window (~03:00 – 05:00);
- (iv) Real-time settlement (05:00 – 18:00);
- (v) End of day (18:00 – 18:45).

CSD System supports RTGS and other settlement methods with intraday finality (technical netting, technical netting with optimisation and a partial settlement). Non-T2S eligible securities registered in CSD System usually will be settled using RTGS method.

Status of settlement will be available to participants through special-purpose client application (GUI of CSD System) and ISO 20022-based messaging.

Q.8.2.4: *If settlement occurs through multiple-batch processing, what is the frequency of the batches and within what time frame do they operate? What happens if a participant does not have enough funds or securities at the settlement time? Are transactions entered in the next batch? If so, what is the status of those transactions and when would they become final?*

Settlement of T2S eligible securities in T2S

T2S offers continuous settlement of T2S eligible securities in two periods: night time settlement (NTS) and real-time settlement (RTGS). NTS takes place in cycles:

- (i) the first night-time cycle including 5 sequences mainly dedicated to settle transactions: cash related (0), CA related (1), FoP related (2), CBO related (3), DvP related (4) and all unsettled transactions from previous sequences;
- (ii) the last night-time cycle, including 4 sequences mainly dedicated to settle transactions: DvP related (4) and unsettled transactions from the previous sequence, with partial (X), multiple liquidity provider related (Y), liquidity transfer related (Z).

If a participant does not have enough funds or securities at the settlement time, for NTS transfer orders are included in the next cycle. Transfer order may be settled partially if:

- (i) partial settlement window is running (for NTS - last NTS cycle, for RTGS – between 15:00 – 15:15 and between 16:45 – 17:00),
- (ii) the settlement instructions are eligible for partial settlement; and
- (iii) the threshold requirement is fulfilled.

Settlement of non-T2S eligible securities in CSD System

CSD System supports the following settlement methods:

- (i) RTGS – settlement instructions are settled in real time;
- (ii) technical netting – instructions are settled only if technical netting is successful;
- (iii) technical netting with optimisation – the batch is settled if the netting is successful. If the netting is not successful, the batch is optimised;
- (iv) partial settlement – partial gross settlement in real time when securities or/cash is not sufficient to settle in full, the settlement instructions are eligible for partial settlement and the threshold requirement is fulfilled.

Details of time frame are provided in the Operating Manual of the Depository.

Q.8.2.5: *If settlement does not occur intraday or in real time, how has the LVPS or SSS considered the introduction of either of these modalities?*

Not applicable.

Key consideration 3: An FMI should clearly define the point after which unsettled payments, transfer instructions, or other obligations may not be revoked by a participant.

Q.8.3.1: *How does the FMI define the point at which unsettled payments, transfer instructions or other obligations may not be revoked by a participant? How does the FMI prohibit the unilateral revocation of accepted and unsettled payments, transfer instructions or obligations after this time?*

Under Section 6.5 of Chapter I of the Rules a Transfer Order is irrevocable from the moment at which the Transfer Order is given a status "matched":

- (i) in the case of T2S eligible securities, on the T2S Platform, or
- (ii) in the case of non-T2S eligible securities, on CSD System.

The status “matched” means that the Transfer Order is or becomes incapable of being amended or cancelled in accordance with the respective T2S or CSD System procedures by a unilateral instruction of the Participant, or any third party, who wishes to have the order amended or deleted. This, however, does not prejudice the right of the Depository to apply contingency measures and to correct errors and reverse entries in exceptional circumstances and the right of the Account Operator to amend the status indicators of a Transfer Order.

See also answer under Q.8.1.1 above regarding the prohibition to revoke transfer orders after the moment of irrevocability under the applicable law.

Q.8.3.2: *Under what circumstances can an instruction or obligation accepted by the system for settlement still be revoked (for example, queued obligations)? How can an unsettled payment or transfer instruction be revoked? Who can revoke unsettled payment or transfer instructions?*

In accordance with the Rules:

- (i) the Participant may unilaterally cancel a submitted Transfer Order until the moment such instruction is matched with a corresponding instruction;
- (ii) matched Transfer Orders may only be cancelled bilaterally with the consent of both Participants . SFD LV shall be amended to allow bilateral cancellation
- (iii) the Depository may enter the cancellation instruction in the CSD System upon the request of the Participant, in respect of Corporate Actions and restrictions and in other cases provided in the Rules and applicable law.
- (iv) the Participants submit a cancellation instruction in the manner and time schedule provided in the Operating Manual. The original settlement instructions are cancelled at the moment when the cancellation instructions are matched in T2S or CSD System, as a case may be. If the original instructions are partly settled, only the outstanding unsettled amount is cancelled.
- (v) Transfer Orders that are not matched within the time schedule provided in the T2S Rules or the Operating Manual are not valid and are automatically cancelled in T2S or CSD System, as a case may be.

Q.8.3.3: *Under what conditions does the FMI allow exceptions and extensions to the revocation deadline?*

The Depository has set the revocation as SF II moment as certain point in the settlement day (please see the response to Q.1.1.3). Revocation deadline is not set as a certain time in the settlement day. According to the Rules in contingency situations the Depository has to use all reasonable efforts to minimise the duration of any interruption for the Participants and shall be entitled, among others, changing the schedule for data processing and settlement activities, including temporary suspension of such activities, extraordinary extension of the working time of the Settlement System(s) and postponing of the Settlement Dates of affected Transfer Orders.

Q.8.3.4: *Where does the FMI define this information? How and to whom is this information disclosed?*

The Rules will be available on the Depository’s official web site.

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Principle 9: Money settlements

An FMI should conduct its money settlements in central bank money where practical and available. If central bank money is not used, an FMI should minimise and strictly control the credit and liquidity risk arising from the use of commercial bank money.

This principle should be reviewed in the context of Principle 8 on settlement finality, Principle 16 on custody and investment risks, and other principles, as appropriate.

Key consideration 1: An FMI should conduct its money settlements in central bank money, where practical and available, to avoid credit and liquidity risks.

Q.9.1.1: *How does the FMI conduct money settlements? If the FMI conducts settlement in multiple currencies, how does the FMI conduct money settlement in each currency?*

General

On the date the authorisation to provide CSD services under CSDR becomes effective the Depository intends to conduct money settlement only in CeBM and only in euro. In future, the Depository may make available:

- (i) settlement of T2S eligible securities in non-euro area central bank currency that is available for settlement on T2S provided that Currency Participation Agreement is concluded between the Eurosystem and a non-euro area central bank.
- (ii) settlement of securities in CoBM in USD or other currencies subject to availability of special purpose credit institution providing such services in the Baltic countries and compliance of such credit institution and the Depository with the CSDR.

Autonomous central bank money model is used for the settlement of cash leg of DvP transfer orders of non-T2S eligible securities.

Settlement of T2S eligible securities in euro via DCAs

Each Participant in T2S designates at least one DCA which is used for the settlement of T2S eligible securities in euros, including corporate actions, on T2S Platform. The DCA so designated is either the DCA maintained by the Participant itself or a Payment Bank in T2S providing cash settlement services for the Participant.

The Depository opens in its name a DCA in T2S which is used for the settlement of corporate action proceeds in euro in respect of T2S eligible securities.

DCAs are linked to external RTGS accounts by the competent central bank.

On the Settlement Day:

- (i) in case of settlement of the cash leg of DvP Transfer Order of T2S eligible securities, the Participant before the deadline set by the Depository ensures that the required cash amount is transferred to the Payment Bank's DCA;
- (ii) in case of distribution of corporate action proceeds in respect to T2S eligible securities the Participant who services the Issuer as soon as the Settlement Day in T2S starts transfers the required cash amount to the Depository's DCA in T2S.

During the Settlement Day the Depository settles:

- (i) the cash leg of DvP Transfer Order of T2S eligible securities by debit of the cash amount from the DCA linked to the buying Participant's securities account and credit to the DCA linked to the selling Participant's securities account;
- (ii) collects corporate action in-turns and distributes corporate action cash out-turns in respect to T2S eligible securities through the Depository's DCA in T2S.

Before the end of a Settlement Day, T2S automatically transfers:

- (i) any remaining cash balance from the Participant's DCA to its RTGS account associated to the DCA;
- (ii) any remaining cash balance from the Depository's DCA to its RTGS account.

Settlement of non-T2S securities in euro via RTGS account and CSA

The Depository opens a RTGS account in T2 Component system which is used for settlement of Transfer Orders in respect of non-T2S eligible securities in euros, including corporate action proceeds. The Depository uses autonomous central bank money model, therefore it maintains CSAs in CSD System in order to account for (i.e. keep sub-bookkeeping records):

- (i) the cash transferred by the Cash Agent to Depository's RTGS account,
- (ii) cash debit in the CSA of delivering Cash Agent or the CSA of the Depository and cash credit in the CSA of receiving Cash Agent or the CSA of the Depository; and
- (iii) cash transferred from the Depository's RTGS account to the cash account of the Cash Agent (liquidity return will create debit of CSA of Cash Agent and credit of mirror cash account of the Depository's RTGS account in CSD System).

On the Settlement Day before the deadline set by the Depository the Participant ensures that the required cash amount is transferred to the Depository's RTGS account. The Depository accounts for the amount credited to its RTGS account in the CSA of the Cash Agent (DvP securities settlement) or the CSA of Depository (corporate action proceeds).

During the Settlement Day the Depository settles the cash leg of non-T2S eligible securities in CSD System:

- (i) in case of **DvP Transfer Order**, by debit of the cash amount from the CSA of the delivering Participant's Cash Agent and credit to the CSA of the receiving Participant's Cash Agent.
- (ii) in case of **corporate action proceeds**, by debit of the cash amount from the Depository's CSA and credit to the CSA of the receiving Participant's Cash Agent (distributing out-turns) and *vice versa* (collecting in-turns).

The Depository transfers the remaining net cash balance of the Cash Agent from the RTGS of the Depository to the RTGS of the respective Cash Agent:

- (i) automatically at the end of the Settlement Day;
- (ii) upon the request of the Cash Agent at any time during the Settlement Day.

Under the Rules settlement of cash transfer is final when the settlement amount is debited from the CSA of the delivering Cash Agent's CSA and credited to the CSA of the receiving Cash Agent.

Q.9.1.2: *If the FMI does not settle in central bank money, why is it not used?*

Not applicable (please see the response under Q.9.1.1 above).

Key consideration 2: If central bank money is not used, an FMI should conduct its money settlements using a settlement asset with little or no credit or liquidity risk.

Q.9.2.1: *If central bank money is not used, how does the FMI assess the credit and liquidity risks of the settlement asset used for money settlement?*

Not applicable.

Q.9.2.2: *If the FMI settles in commercial bank money, how does the FMI select its settlement banks? What are the specific selection criteria the FMI uses?*

Not applicable.

Key consideration 3: If an FMI settles in commercial bank money, it should monitor, manage, and limit its credit and liquidity risks arising from the commercial settlement banks. In particular, an FMI should establish and monitor adherence to strict criteria for its settlement banks that take account of, among other things, their regulation and supervision, creditworthiness, capitalisation, access to liquidity, and operational reliability. An FMI should also monitor and manage the concentration of credit and liquidity exposures to its commercial settlement banks.

Q.9.3.1: *How does the FMI monitor the settlement banks' adherence to criteria it uses for selection? For example, how does the FMI evaluate the banks' regulation, supervision, creditworthiness, capitalisation, access to liquidity and operational reliability?*

Not applicable.

Q.9.3.2: *How does the FMI monitor, manage and limit its credit and liquidity risks arising from the commercial settlement banks? How does the FMI monitor and manage the concentration of credit and liquidity exposures to these banks?*

Not applicable. CSDR provides special prudential framework for use of commercial bank money: use of special purpose credit institution as a settlement agent is subject to strict prudential and risk management requirements.

Q.9.3.3: *How does the FMI assess its potential losses and liquidity pressures as well as those of its participants if there is a failure of its largest settlement bank?*

Not applicable.

Key consideration 4: If an FMI conducts money settlements on its own books, it should minimise and strictly control its credit and liquidity risks.

Q.9.4.1: *If an FMI conducts money settlements on its own books, how does it minimise and strictly control its credit and liquidity risks?*

The Depository does not conduct money settlements on its own books. However, the Depository maintains CSAs in CSD System in order to account for (i.e. keep sub-bookkeeping records):

- (i) the cash transferred by the Cash Agent to Depository's RTGS account;
- (ii) cash debit in the CSA of delivering Cash Agent or the CSA of the Depository and cash credit in the CSA of receiving Cash Agent or the CSA of the Depository; and
- (iii) cash transferred from the Depository's RTGS account to the cash account of the Cash Agent (see answer under Q. 9.1.1 above).

Key consideration 5: An FMI's legal agreements with any settlement banks should state clearly when transfers on the books of individual settlement banks are expected to occur, that transfers are to be final when effected, and that funds received should be transferable as soon as possible, at a minimum by the end of the day and ideally intraday, in order to enable the FMI and its participants to manage credit and liquidity risks.

Q.9.5.1: *Do the FMI's legal agreements with its settlement banks state when transfers occur, that transfers are final when affected, and that funds received are transferable?*

See answer under Q. 9.1.1 above.

Q.9.5.2: *Are funds received transferable by the end of the day at the latest? If not, why? Are they transferable intraday? If not, why?*

See answer under Q. 9.1.1 above

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Principle 11: Central securities depositories

A CSD should have appropriate rules and procedures to help ensure the integrity of securities issues and minimise and manage the risks associated with the safekeeping and transfer of securities. A CSD should maintain securities in an immobilised or dematerialised form for their transfer by book entry.

In reviewing this principle, where an entity legally defined as a CSD or an SSS does not hold or facilitate the holding of assets or collateral owned by its participants, the CSD or SSS in general would not be required to have arrangements to manage the safekeeping of such assets or collateral. This principle should be reviewed in the context of Principle 17 on operational risk, Principle 20 on FMI links, and other principles, as appropriate.

Key consideration 1: A CSD should have appropriate rules, procedures, and controls, including robust accounting practices, to safeguard the rights of securities issuers and holders, prevent the unauthorised creation or deletion of securities, and conduct periodic and at least daily reconciliation of securities issues it maintains.

Safeguarding the rights of securities issuers and holders

Q.11.1.1: *How are the rights of securities issuers and holders safeguarded by the rules, procedures and controls of the CSD?*

The Rules and the applicable law provide, among others, the following safeguards with respect to the issuers and holders:

- (i) securities accounting requirements applicable to the top tier accounts with any Settlement System and, in case of nominee accounts, a second tier accounts maintained by the Account Operator in its own books (refer to the answer under Q.11.1.3 below);
- (ii) asset segregation requirements (referred to the answer under Q.11.5 below);
- (iii) prohibition for the Depository to use on its own account the securities of the account holder without a prior written consent of the account holder. The Rules provide for a procedure to obtain consent from the account holder in compliance with Article 38(7) of the CSDR;
- (iv) internal control system, including organisational requirements (i.e. separation of duties), system controls and checks; and
- (v) proper reconciliation on a daily basis in compliance with the CSDR and technical standards under the CSDR (refer to the answer under Q. 11.1.5 below);

- (vi) the liability of the Depository vis-a-vis the Participants and the Issuers and *vice versa* is clearly defined in the Rules;
- (vii) civil liability rules of the registrar of the ECRS, including mandatory liability insurance of the ECSD and Liability of the Republic of Estonia in accordance with § 52 of ECRS Act;
- (viii) risks of the Depository will be insured by professional indemnity insurance (errors and omissions) and directors and officers insurance in accordance with Nasdaq Group insurance policy.

Q.11.1.2: *How do the CSD's rules, procedures and controls ensure that the securities it holds on behalf of participants are appropriately accounted for on its books and protected from risks associated with the other services the CSD may provide?*

Main account types

Under Section 5.3. of Chapter I of the Rules the Depository opens and keeps records of the following main types of Operational Accounts that enable keeping corresponding securities accounts in one or more Settlement Systems:

- (i) **owner account** - an account that is registered in the name of the customer (individual or legal entity) of the Account Operator and is used for holding securities owned by that customer;
- (ii) **participant own account** – an account that is registered in the name of the Account Operator and is used for holding securities owned by the Account Operator;
- (iii) **omnibus account** - an account that is opened (i) in the name of an Account Operator for holding securities of the Account Operator’s multiple customers; or (ii) in the name of a Foreign CSD for holding securities under a CSD link arrangement between the Depository and Foreign CSD.
- (iv) **nominee account** - an account that is registered in the name of a customer of an Account Operator and is used for holding securities of multiple clients of such customer, regardless of whether such clients are end investors or act as intermediaries in the securities holding chain.
- (v) **segregated nominee account** - an account that is registered in the name of an Account Operator or a customer of the Account Operator (each referred to as “segregated nominee account holder”) and is used for holding securities for a single customer of the segregated nominee account holder, regardless of whether such customer is the end investor or acts as an intermediary in the securities holding chain.

Omnibus accounts, nominee accounts and segregated nominee accounts are subject to two level securities accounting requirements set out in the Rules and the applicable law.

Owner accounts ensure individual client segregation in accordance with Article 38 (4) of the CSDR.

Insolvency protection

Insolvency of the Depository

If the authorisation of the Depository is revoked due to commencement of insolvency proceedings, the Depository makes the necessary arrangements with another authorised CSD in order to transfer the assets of the account holders and the corresponding securities account records to such CSD in compliance with Article 20(5) of the CSDR and other applicable rules, procedures and authorisations of the FSA (if any).

Q.11.1.3: *How does the CSD ensure that it has robust accounting practices? Do audits review whether there are sufficient securities to satisfy customer rights? How frequently are end-to-end audits conducted to examine the procedures and internal controls used in the safekeeping of securities?*

Common provisions

The securities accounting system for omnibus accounts, nominee accounts and segregated nominee accounts consist of:

- (i) First level – securities accounting by the Depository in respect of top tier securities accounts;
- (ii) Second level – securities accounting by the Account Operator or respective client of Account Operator in respect of second tier securities accounts.

The Depository and the Account Operator are responsible for maintaining adequate securities records in accordance with the Rules and the applicable law. At the first level the Depository performs securities accounting according to the law that applies to the Settlement System in which omnibus accounts, nominee accounts or segregated nominee account are held.

At the second level the account holder performs securities accounting according to the Rules and the law that applies to the second tier securities account:

- (i) for accounts located in Estonia - Estonian law is applicable;
- (ii) for accounts located in Latvia – Latvian law is applicable;
- (iii) for accounts located in Lithuania - Lithuanian law is applicable.

The Depository ensures compliance by the Account Operators with robust securities accounting practices through well documented rules of procedure, qualified personnel, systems and controls, and IT systems.

Country specific provisions

Furthermore, if the Account Operator is a Latvian credit institution or an investment brokerage company, it has to ensure that a sworn auditor at least once a year inspects whether the measures taken by such Account Operator are sufficient to meet the securities protection requirements provided in the Latvian Financial Instruments Market Law (e.g. segregation of securities held on own account and on the account of clients, prohibition to use client securities on own account without prior consent). The sworn auditor has to submit a written report to the FCMC regarding the results of such inspection (*Article 129² of the Financial Instruments Market Law*).

Owner accounts

Records of owner accounts are kept by the Depository in the Settlement System in which the securities account is opened. Two level securities accounting requirements do not apply to the transparent (direct) holding model whereby the owner accounts are maintained by the Account Operator but securities records are kept by the Depository.

Prevention of the unauthorised creation or deletion of securities

Q.11.1.4: *What are the CSD's internal procedures to authorise the creation and deletion of securities? What are the CSD's internal controls to prevent the unauthorised creation and deletion of securities?*

Only authorised employees of the Depository can create or delete securities and do that on a basis of documented application from the Issuer or other authorised party and after respective decision by Management Board has been made. These entries are made on the basis of 4-eye-principle.

Validation and settlement engine of CSD System is developed so that:

- (i) Account Operators cannot transfer more securities than in the respective securities account (no debit balances); and
- (ii) the transfer instruction is automatically rejected by the Depository if the ISIN used is not registered with the respective Settlement System (no creation of securities).

In case of nominee accounts, the Account Operators are responsible for arrangements to prevent unauthorised creation and deletion of securities that are recorded in their own books.

Periodic reconciliation of securities issues

Q.11.1.5: *Does the CSD conduct periodic and at least daily reconciliation of the totals of securities issues in the CSD for each issuer (or its issuing agent)? How does the CSD ensure that the total number of securities recorded in the CSD for a particular issue is equal to the amount of securities of that issue held on the CSD's books?*

The Depository conducts periodic and at least daily reconciliation measures to verify that the number of securities making up a securities issue or part of a securities issue submitted to the CSD is equal to the sum of securities recorded on the securities accounts of the participants of the Settlement Systems in accordance with Article 37(1) of the CSDR and the technical standards adopted by the European Commission on the basis of the CSDR. In order to ensure compliance of the Participants with the requirements regarding the integrity of securities issue, according to the Rules the Depository *inter alia* may:

- (i) request that Participant(s) apply specific event-driven reconciliation measure(s) in a manner specified by the Depository;
- (ii) subject Participant(s) to audit control on the application of reconciliation measures.

According to the Rules the Depository makes available to the Account Operator, the holder of owner account, the Issuer, the Issuer Agent and the Fund Administrator information and statements relating to the Operational Account, securities account, Issuance Account and the Distribution Account, respectively, in accordance with in the Operating Manual. The Account Operator, the Issuer, the Issuer Agent and the Fund Administrator are responsible for reconciling their records of securities accounts with the account statements provided by the Depository and to inform the Depository of any error or omission in the information with respect to any securities account or Issuance Account it becomes aware of.

Q.11.1.6: *If the CSD is not the official registrar of the issues held on its books, how does the CSD reconcile its records with official registrar?*

The Depository acts as official registrar of all issues with Estonian ISIN codes. The Depository also assigns Latvian and Lithuanian ISIN codes to securities initially registered with the Latvian Settlement System and Lithuanian Settlement System, respectively. For issues to which the Depository acts as investor CSD daily reconciliation of foreign securities (non-Estonian/Latvian/Lithuanian ISINs) is conducted in accordance with the technical standards adopted by the European Commission on the basis of the CSDR.

Key consideration 2: A CSD should prohibit overdrafts and debit balances in securities accounts.

Q.11.2.1: *How does the CSD prevent overdrafts and debit balances in securities accounts?*

Overdrafts and debit balances in securities accounts with any Settlement System are not possible due to technical and functional controls in CSD System and provisions of the Rules that require that the Participants maintain sufficient balance of securities to effect debit and subsequent credit to the securities account.

Key consideration 3: A CSD should maintain securities in an immobilised or dematerialised form for their transfer by book entry. Where appropriate, a CSD should provide incentives to immobilise or dematerialise securities.

Q.11.3.1: *Are securities issued or maintained in a dematerialised form? What percentage of securities is dematerialised, and what percentage of the total volume of transactions applies to these securities?*

Yes, securities are maintained in dematerialised form (please refer to the answer under Q.1.1.3 (a) regarding legal basis for the dematerialisation.

On the date of this self-assessment:

- (i) 100% of securities registered in ECSR are in a dematerialised form and it is planned that this ratio will not materially differ for the Estonian Settlement System;
- (ii) 100% of securities issued in public circulation registered with CSD LV as Issuer CSD are in dematerialised form, and it is planned that this ratio will not materially differ for the Latvian Settlement System;
- (iii) 100% of securities registered with CSD LT as Issuer CSD are in dematerialised form, and it is planned that this ratio will remain unchanged for the Lithuanian Settlement System.

All transfers of securities in all Settlement Systems are executed in book entry form only.

Q.11.3.2: *If securities are issued as a physical certificate, is it possible to immobilise them and allow their holding and transfer in a book-entry system? What percentage of securities is immobilised, and what percentage of the total volume of transactions applies to immobilised securities?*

The Depository may record physical certificates in any Settlement System in book entry form after their immobilisation with the Depository in accordance with Article 3 of the CSDR and the procedure set out in the agreement between the Depository, on the one hand, and the Issuer or the owner of securities, on the other hand.

On the date of this self- assessment there are no immobilised securities recorded in CSD LV, CSD LT and CSD EE.

Q.11.3.3: *What incentives, if any, does the CSD provide to immobilise or dematerialise securities?*

Please refer to the answer under Q. 11.3.1 and Q. 11.3.2 above.

The Depository may record physical certificates in book entry form in any Settlement System after their immobilisation with the Depository.

Key consideration 4: A CSD should protect assets against custody risk through appropriate rules and procedures consistent with its legal framework.

Q.11.4.1: *How do the CSD's rules and procedures protect assets against custody risk, including the risk of loss because of the CSD's negligence, misuse of assets, fraud, poor administration, inadequate recordkeeping or failure to protect participants' interests in their securities?*

Please refer to answers under Q. 11.1.1 and Q. 11.1.2 explaining the structure of relationship and the main components of protection of securities held with the Settlement Systems.

Q.11.4.2: *How has the CSD determined that those rules and procedures are consistent with the legal framework?*

The Depository's local legal counsels are responsible for ensuring that the rules and procedures of the respective Settlement System comply with the applicable law. Further, the Depository is an authorised entity and it is audited by the respective competent authority (FCMC) on annual bases.

Q.11.4.3: *What other methods, if any, does the CSD employ to protect its participants against misappropriation, destruction and theft of securities (for example, insurance or other compensation schemes)?*

The Rules prohibits the Depository from using on its own account the securities of the account holder without a prior written consent of the account holder. The Rules provide a procedure for obtaining such consent in compliance with 38(7) of the CSDR. Please refer to answer under Q. 11.1.1 regarding insurance of the Depository's liability in case of misappropriation, destruction or theft of securities.

Key consideration 5: A CSD should employ a robust system that ensures segregation between the CSD's own assets and the securities of its participants and segregation among the securities of participants. Where supported by the legal framework, the CSD should also support operationally the segregation of securities belonging to a participant's customers on the participant's books and facilitate the transfer of customer holdings.

Q.11.5.1: *What segregation arrangements are in place at the CSD? How does the CSD ensure segregation between its own assets and the securities of its participants? How does the CSD ensure segregation among the securities of participants?*

The Depository keeps records and offers top tier securities account types in any Settlement System that enable it at any time and without delay to segregate in such accounts the securities of an account holder from those of any other account holder. The Depository does not directly hold its own securities on its own account; such assets are held via a System Participant (asset segregation under *Article 38(1) of the CSDR*).

Account Operator wishing to hold securities in top tier securities account on its own account opens a participant own account which is used for holding securities which are owned by the Account Operator (asset segregation under *Article 38(2) of the CSDR*).

The clients of Account Operators may choose the preferred level of asset segregation by choosing between the following top-tier securities accounts: (i) omnibus account (which is used to achieve omnibus client segregation under *Article 38(3) of CSDR*), (ii) owner account, (iii) segregated nominee account or (iv) nominee account ((ii) to (iv) are used to achieve individual client segregation under *Article 38(4) of CSDR*). The Depository keeps records that correspond to the account types of the holders of securities accounts with the respective Settlement System.

Foreign CSD acting as Investor CSD may open an omnibus nominee Operational Account with one or more Settlement Systems in order to hold securities registered with the respective Settlement System.

Q.11.5.2: *Where supported by the legal framework, how does the CSD support the operational segregation of securities belonging to participants' customers from the participants' book? How does the CSD facilitate the transfer from these customers' accounts to another participant?*

Following main types of accounts (see response to Q 11.1.2 for more detailed explanation of account types) can be used, thanks to Rules and functionality of CSD System, by Account Operators and other System participants to segregate securities belonging to participants' customers from the participants' book.

The Depository's Rules and functionality of CSD System allow an investor to migrate from one Account Operator to another by way of transfer of total balance of all securities (different ISINs) from the original owner account to a new owner account (opened in the name of the same person but through different Account Operator). Further, Rules and functionality of CSD System allow investor to migrate its holdings from owner account to omnibus account of the Account Operator.

Key consideration 6: A CSD should identify, measure, monitor, and manage its risks from other activities that it may perform; additional tools may be necessary in order to address these risks.

Q.11.6.1: *Does the CSD provide services other than central safekeeping and administration of securities and settlement? If so, what services?*

All Settlement Systems

The Depository processes corporate action for the securities initially recorded in any Settlement System.

Estonia

Currently, CSD EE manages mandatory pension system which is a substantially similar service to central safekeeping of securities. Depending on legislative developments in Estonia, this business might be transferred from CSD EE to an Estonian subsidiary of CSD EE in the course of cross-border merger of the Baltic CSDs.

Latvia

The Depository keeps the initial register of shareholders (“**Initial Register**”) for privatized companies until the owners of securities have opened a securities account with a System Participant to the Latvian Settlement System. The Depository maintains Initial Register in accordance with Chapter III of the Rules and the relevant provisions of the Financial Instruments Market Law.

The Depository also maintains savings notes registry accounts in accordance with the Cabinet of Ministers Regulations No. 237 of 6 May 2014 “Regulations on the Issue of Government Securities”, its rules and agreements with the State Treasury.

Lithuania

The Depository will provide retail government bonds (savings notes) services which include:

- (i) registration of retail government bond issues for retail distribution via web service;
- (ii) maintenance of securities database in web service and balancing with the Lithuanian Settlement System;
- (iii) handling of retail government bonds subscription and redemption requests in web service and balancing with related cash flows in payment systems and commercial banks.

Q.11.6.2: *If the CSD provides services other than central safekeeping and administration of securities and settlement, how does it identify the risks associated with those activities, including potential credit and liquidity risks? How does it measure, monitor and manage these risks, including legally separating services other than safekeeping and administration of securities where necessary?*

Latvia

According to the Financial Instruments Market Law, if the Depository holds cash (corporate action proceeds) in custody for the owners of securities that are registered in the Initial Register or were registered in the Initial Register and on the last day of the term for the final share buyback offer had not accepted the offer, the Depository:

- (i) holds such cash with the Bank of Latvia separately from its own cash;
- (ii) may invest such cash only in securities issued by the EU/EEA Member States or other low risk debt securities and use the income (interest) from such investment;
- (iii) must not use such cash in order to satisfy the claims of the Depository's creditors, including in the course of insolvency proceedings of the Depository.

The Depository manages potential risks associated with registration and handling of savings notes through robust procedures, professional insurance and agreement with the State Treasury.

Lithuania

The Depository manages potential risks associated with registration and handling of savings notes through robust procedures, professional insurance and contracts between the Depository and the service users.

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Principle 12: Exchange-of-value settlement systems

If an FMI settles transactions that involve the settlement of two linked obligations (for example, securities or foreign exchange transactions), it should eliminate principal risk by conditioning the final settlement of one obligation upon the final settlement of the other.

This principle should be reviewed in the context of Principle 4 on credit risk, Principle 7 on liquidity risk, Principle 8 on settlement finality, and other principles, as appropriate.

Key consideration 1: An FMI that is an exchange-of-value settlement system should eliminate principal risk by ensuring that the final settlement of one obligation occurs if and only if the final settlement of the linked obligation also occurs, regardless of whether the FMI settles on a gross or net basis and when finality occurs.

Q.12.1.1: *How do the FMI's legal, contractual, technical and risk management frameworks ensure that the final settlement of relevant financial instruments eliminates principal risk? What procedures ensure that the final settlement of one obligation occurs if and only if the final settlement of a linked obligation also occurs?*

T2S accepts linked settlement instructions with respect to T2S eligible securities. Linked instructions are subject to specific rules during business validation and settlement process which are set out in T2S User Guide.

A link can be created between two settlement instructions, two settlement restrictions, between a settlement instruction and a settlement restriction or a pool of instructions. T2S allows linking settlement instructions in two ways.

1. Settlement instruction is linked to another settlement instruction with a processing code corresponding to:

- (i) Before (BEFO) – the settlement instruction must be settled before or at least at the same time as the linked instruction (e.g. linked securities receipt in buy-in of securities intended for redelivery);

- (ii) After (AFTE) – the settlement instruction must be settled after or at least at the same time as the linked instruction (e.g. linked securities redeliveries in back-to-back transactions);
- (iii) All-or-none (WITH) – the settlement instruction must be settled at the same time with the linked instruction (e.g. linking together several transactions composing a corporate action);
- (iv) Information (INFO) – the settlement instructions are linked for informational purposes only. There is no processing applied to informational links.

2. A Pool Reference – the settlement instruction is added to a uniquely identified pool (group) of settlement instructions to be settled on all-or-none basis.

Transactions linked by T2S users are not eligible for partial settlement.

Q.12.1.2: *How are the linked obligations settled - on a gross basis (trade by trade) or on a net basis?*

Linked obligations are settled on a gross basis.

Q.12.1.3: *Is the finality of settlement of linked obligations simultaneous? If not, what is the timing of finality for both obligations? Is the length of time between the blocking and final settlement of both obligations minimised? Are blocked assets protected from a claim by a third party?*

Yes, finality of settlement of linked obligations is virtually simultaneous.

Q.12.1.4: *In the case of a CCP, does the CCP rely on the DvP or PvP services provided by another FMI, such as an SSS or payment system? If so, how would the CCP characterise the level of its reliance on such services? What contractual relationship does the CCP have with the SSS or payment system to ensure that final settlement of one obligation occurs only when the final settlement of any linked obligations occurs?*

Not applicable.

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Principle 13: Participant-default rules and procedures
 An FMI should have effective and clearly defined rules and procedures to manage a participant default. These rules and procedures should be designed to ensure that the FMI can take timely action to contain losses and liquidity pressures and continue to meet its obligations.

Because of the extensive interactions between the default management principles as they apply to CCPs, this principle needs to be reviewed in the context of Principle 14 on segregation and portability. This principle should also be reviewed in the context of Principle 4 on credit risk, Principle 7 on liquidity risk, Principle 23 on disclosure of rules, key procedures and market data, and other principles, as appropriate.

Key consideration 1: An FMI should have default rules and procedures that enable the FMI to continue to meet its obligations in the event of a participant default and that address the replenishment of resources following a default.

Participant default rules and procedures

Q.13.1.1: *Do the FMI's rules and procedures clearly define an event of default (both a financial and an operational default of a participant) and the method for identifying a default? How are these events defined?*

Financial default

According to the Rules **default of a Participant** means any and all circumstances that may cause a situation where a Participant is not, due to its solvency, change in legal status, technical interruption or restrictions on its activity established against it, able to perform its obligations in connection with its participation in the Settlement System(s) of the Depository (“Default Event”).

As regards identification of the commencement of insolvency proceedings, the relevant laws provide:

- (i) in respect of **Estonian Settlement System**, a member of the system or linked system shall immediately notify the system or linked system operator and the Estonian FSA of the initiation and termination of bankruptcy proceedings against it or if it is declared bankrupt or a moratorium is established with respect to it. The same obligation also rests with the interim trustee in bankruptcy, the trustee in bankruptcy or the moratorium administrator with respect to a member of the system or linked system (*§ 228 (6) of the SMA*).
- (ii) in respect of **Latvian Settlement System**, the FCMC is informed on the commencement of insolvency proceedings of a participant (i) by a court in accordance with the Civil Procedure Law or (ii) immediately on the same day by a competent authority that has made a decision on commencement of insolvency proceedings. FCMC immediately on the day when it has received a decision by a Latvian court or a competent authority regarding commencement of insolvency proceedings has to inform about this the operators of the systems in which the participant is a member, institutions designated by the EU Member States and notified to the European Commission for receipt of such information, the European Systemic Risk Board and ESMA (*Article 11 of SFD LV*).
- (iii) in respect of **Lithuanian Settlement System**, if the court has initiated bankruptcy proceedings against, or the court or other institution has taken a decision on the suspension of operation of, a system participant registered in Lithuania, the court or other institution has to immediately notify the Bank of Lithuania about such proceedings. The decision of the court or other institution has to provide the calendar date and hour of taking decision. Upon the receipt of the notification from (i) the court or other institution referred to above or (ii) a competent institution of another EU Member State about the suspension of operations of the participant to the system whose participants have chosen Lithuanian law as the law applicable to the rights and obligations resulting from the participation in the system, or bankruptcy proceedings initiated against it, the Bank of Lithuania immediately notifies the operator of that system. (*Article 8(1)-(3) of SFD LT*).

Operational default

According to the Rules **operational default** means material interruption of services provided by the Depository in connection with its Settlement System for any reason, including as a result of a software error, telecommunications outage or Default Event of the Participant(s). In case of operational default, the Depository has to use all reasonable efforts to minimise the duration of any interruption for the Participants and has a right to apply the following contingency measures:

- (i) changing the schedule for data processing and settlement activities, including temporary suspension of such activities, extraordinary extension of the working time of the Settlement System(s) and postponing of the Settlement Dates of affected transfer orders;
- (ii) temporary restriction of access to the Settlement System or certain functionalities thereof;
- (iii) forwarding transfer orders and other instructions issued for performing CSD activities of the Depository through alternative communication channels and, if necessary, manual processing of transfer orders and instructions so forwarded; and

- (iv) other measures foreseen in the recovery plan of the Depository notified to the Participants or respective System Participants of the affected Settlement System.

Q.13.1.2: *How do the FMI's rules and procedures address the following key aspects of a participant default:*

a) the actions that the FMI can take when a default is declared;

In case insolvency proceedings of a Participant are commenced, the Depository takes the following measures:

- (i) rejects new transfer orders from the defaulting Participant and blocks the communication means with CSD System available to the Participant. If the Participant is a DCP, the Depository also blocks/suspends its set-up in T2S;
- (ii) handles the existing transfer orders of the defaulting Participant that are submitted for settlement to the Depository in accordance with the Rules ; and
- (iii) revokes the Participant's status in accordance with the Rules. In particular, the Depository may at any time unilaterally terminate the participation agreement(s) with a Participant, for all or part of the services and functionalities, with effect from such date and time as the Depository may specify.

In case of **Estonian Settlement System**, the following safeguards apply:

- (i) the Depository has to immediately stop accepting transfer orders from defaulting participant (§ 228 (1) of the SMA).
- (ii) the initiation of bankruptcy proceedings against a member of the system or linked system or a third party that provided a collateral to a member of the linked system, and the establishment of a moratorium with respect to a member of the system or linked system which is a credit institution does not suspend the execution of transfer orders forwarded by the relevant member of the system or linked system in accordance with the system or linked system rules to the system or linked system operator prior to the initiation of bankruptcy proceedings or establishment of a moratorium. Obligations undertaken by participating in the system or linked system prior to the initiation of bankruptcy proceedings or establishment of a moratorium shall be performed on account of the collateral established by the member of the system or linked system and the system or linked system guarantee fund (§ 228 (2) of the SMA).

In case of **Latvian Settlement System**, commencement of insolvency proceedings of a participant does not affect the rights and obligations of the participant (including of the participant or the operator of an interoperating system which is not a participant) which arise from, or are connected to, the participation to the system and have arisen before the commencement of insolvency proceedings. Such rights and obligations cannot be declared to be invalid (*Article 12 of SFD LV*).

In case of **Lithuanian Settlement System**, the following safeguards apply:

- (i) the Depository as an operator of the Lithuanian Settlement System, upon being notified that the operations of a System Participant are suspended and/or bankruptcy proceedings are initiated against it, has to take all measures to prevent transfer orders submitted to the Lithuanian Settlement System by that participant from being entered into the Lithuanian Settlement System (*Article 7(3) of SFD LT*);
- (ii) bankruptcy proceedings do not have an effect on performing the rights and obligations of the system participant arising from its participation in the system before the initiation of bankruptcy proceedings (*Article 8(4) of the SFD LT*).

b) the extent to which the actions are automatic or discretionary;

Actions of the Depository are rather automatic.

c) changes to normal settlement practices;

Any default situation may be qualified as an event or circumstance that influences the uninterrupted functioning of the Settlement System within the meaning of provisions of the Rules.

In case of necessity, the Depository may make minor adjustments to the schedule for data processing activities, including temporarily suspend the data processing activities, extraordinary extend the working time of the Settlement System and postpone the Settlement Dates of the affected transfer orders (please refer to the answer under Q. 13.1.1 above).

d) the management of transactions at different stages of processing;

Please refer to answer under c) above.

e) the expected treatment of proprietary and customer transactions and accounts;

The Depository does not differentiate between customer and proprietary transactions. However, transfer orders may have different priority levels (e.g. exchange transactions have higher priority than OTC transactions) under the rules of the Depository. By using settlement priority levels, settlement instructions compete for using the same securities and/or cash.

Priority and sequencing rules are provided in the Service Description of the Depository.

f) the probable sequencing of actions;

Priority and sequencing rules are provided in the Service Description of the Depository. The Depository will apply these rules also upon occurrence of Default Event.

g) the roles, obligations and responsibilities of the various parties, including non-defaulting participants; and

The roles, obligations and responsibilities are set out in the rules of procedure of settlement department and determined according to the Business Continuity Plan. This includes notification templates and contact list of recipients.

h) the existence of other mechanisms that may be activated to contain the impact of a default?

A special guarantee fund is set up Baltic Stock Exchange that may be used in case of default of a member of the respective Baltic Stock Exchange. In particular, transactions that are concluded or registered on any trading venue operated by the Baltic Stock Exchange but cannot be executed due to the insolvency of a member of the respective Baltic Stock Exchange or delayed settlement of the transfer order may endanger regular and reliable continuous and safe operation of the regulated market are managed by the respective Baltic Stock Exchange in accordance with the rules on the formation and the use of the guarantee fund of the respective Baltic Stock Exchange. The rules also provide for a default waterfall mechanism regarding the distribution of the guarantee fund.

Rules and regulations of each Baltic Stock Exchange:

- (i) entitle the Baltic Stock Exchange to impose general or member-specific settlement limits or trading restrictions (*ex-ante* preventive measure);

- (ii) provide deployment regime of the Baltic Stock Exchange guarantee fund (used for ensuring settlement of automatically matched exchange transactions in case of Baltic Stock Exchange member's insolvency, risk to regular functioning of the market or other cases specified in the rules);
- (iii) authorize the Baltic Stock Exchange for the application buy-in and sell-out procedures.

Use of financial resources

Q.13.1.3: *How do the FMI's rules and procedures allow the FMI to promptly use any financial resources that it maintains for covering losses and containing liquidity pressures arising from default, including liquidity facilities?*

The Depository does not guarantee the transfer of funds or securities in any of the Settlement Systems. According to the Rules, the Participant has to take all the necessary measures to ensure smooth and timely settlement of every securities transaction on the ISD. The Participant has to send the instructions to the Settlement System only if the securities to be delivered or the cash balance due are available in the relevant account. The Payment Banks, however, may access central bank auto-collateralisation through T2S in accordance with T2S Rules and the rules of the relevant central bank in order to obtain intraday credit to cover a lack of cash for securities instruction settlement that is secured with eligible collateral.

In addition, Estonian law provides the following safeguards with respect to the **Estonian Settlement System**:

- (i) the registrar of the ECRS acting in the capacity of an operator of a Settlement System, does not have the right to guarantee the performance of claims and obligations arising on the basis of transfer orders (§ 272 (2) of the SMA).
- (ii) the initiation of bankruptcy proceedings against a member of the system or linked system or a third party that provided a collateral to a member of the linked system, and the establishment of a moratorium with respect to a member of the system or linked system which is a credit institution does not suspend the execution of transfer orders forwarded by the relevant member of the system or linked system in accordance with the system or linked system rules to the system or linked system operator prior to the initiation of bankruptcy proceedings or establishment of a moratorium. Obligations undertaken by participating in the system or linked system prior to the initiation of bankruptcy proceedings or establishment of a moratorium shall be performed on account of the collateral established by the member of the system or linked system and the system or linked system guarantee fund (§ 228 (2) of the SMA).

Furthermore, Latvian law provides that commencement of insolvency proceedings of a participant to the **Latvian Settlement System** or interoperable system does not prevent:

- (i) to use the funds available in the settlement account or financial instruments to enable the participant to fulfil the obligations arising from its participation in the system or interoperable system that are outstanding at the business day of commencement of insolvency proceedings; and
- (ii) to reduce the participant's credit related to the system against the collateral available in the system or interoperable system in order to fulfil the obligations of the participant in the respective system.

Lithuanian Law on Markets in Financial Instruments in respect of the **Lithuanian Settlement System** provides a fundamental principle that the operator of the system does not guarantee transfer of funds or securities.

Q.13.1.4: *How do the FMI's rules and procedures address the order in which the financial resources can be used?*

Under the Rules of the Depository transfer orders may have different priority levels (e.g. exchange transactions have higher priority than OTC transactions). In the absence of cash, transactions with higher priority are settled first considering also sequencing rules (which may remain unsettled unless Baltic Stock Exchange guarantee fund is used in the event of exchange transactions and subject to discretion of the respective Baltic Stock Exchange).

As regards settlement of **T2S eligible securities** in T2S, during the settlement of settlement instructions, settlement restrictions or liquidity transfers, T2S uses optimising application processes in a way to increase the number and value of transactions settled in T2S according to the available resources. These application processes rely on the following optimisation tools:

- (i) technical netting which limits the resources needed for their settlement to the net quantities or amounts of settlement instructions, settlement restrictions and liquidity transfers submitted together to a settlement on an all-or-none basis;
- (ii) prioritisation which allows T2S Actors to indicate the settlement instructions and settlement restrictions to settle first in case of resources shortage;
- (iii) partial settlement which allows T2S, under specific conditions, to settle only a part of settlement instructions, settlement restrictions or liquidity transfers with the available resources;
- (iv) auto-collateralisation which allows (a) the provision of intraday credit by central banks and payment/settlement banks for the settlement of settlement instruction in case of lack of cash or insufficient external guarantee headroom and (b) the automatic release of collateral and automatic substitution in order to cover lack of securities;
- (v) optimisation algorithms which allow the identification and selection of pending settlement instructions, settlement restrictions able to settle with success when they are submitted together to a settlement attempt.

As regards settlement of non-T2S eligible securities in CSD System, during the settlement of settlement instructions, settlement restrictions or liquidity transfers, CSD System uses optimising processes in a way to increase the number and value of transactions settled considering the available resources, such as

- (i) technical netting which is used to limit the resources needed for settlement by grouping settlement instructions and calculating net quantities and amounts to be settled on an all or none basis. Available resources are checked against the net quantities and amounts and thereby reduce the resource needed for settlement.
- (ii) settlement prioritisation which allows the participants indicate the settlement instructions and to settle first in case of resources shortage;
- (iii) partial settlement which allows CSD System, under specific conditions, to settle only a part of settlement instructions with the available resources.

Priority and sequencing rules are provided in the Service Description of the Depository.

Q.13.1.5: *How do the FMI's rules and procedures address the replenishment of resources following a default?*

The Depository does not guarantee the transfer of funds or securities in any of the Settlement Systems. Under Section 6.17. of Chapter I of the Rules, the Participant has to send the instructions to the Settlement System only if the securities to be delivered or the cash balance due are available in the relevant account. Consequently, the Rules do not provide for replenishment of resources following the participant's default.

Key consideration 2: An FMI should be well prepared to implement its default rules and procedures, including any appropriate discretionary procedures provided for in its rules.

Q.13.2.1: *Does the FMI's management have internal plans that clearly delineate the roles and responsibilities for addressing a default? What are these plans?*

Roles and responsibilities are covered by rules of procedure of settlement department of each Settlement System and determined according to the Business Continuity Plan. This includes notification templates and contact list of recipients. The procedures for addressing a default are set out in the answer provided under Q.13.1.2 above.

Q.13.2.2: *What type of communication procedures does the FMI have in order to reach in a timely manner all relevant stakeholders, including regulators, supervisors and overseers?*

After the occurrence of Default Event the Depository distributes a circular letter notifying the affected stakeholders about the relevant details.

Q.13.2.3: *How frequently are the internal plans to address a default reviewed? What is the governance arrangement around these plans?*

The internal plans are reviewed upon necessity to reflect the changes from the change of daily practices or rules and regulations. The minimum requirement is to review the internal plans on a yearly basis.

Key consideration 3: An FMI should publicly disclose key aspects of its default rules and procedures.

Q.13.3.1: *How are the key aspects of the FMI's participant default rules and procedures made publicly available? How do they address:*

All aspects of the Depository's participant default rules and procedures are provided in the Rules and Annex II thereto (Default Rules) and the Rules will be publicly available on the official website of the Depository. These rules include:

- (i) the circumstances in which the Depository may take an action;
- (ii) who may take the action;
- (iii) the scope of the actions which may be taken in the event of the participant's default;
- (iv) the mechanisms to address Depository's obligations to non-defaulting participants.

a) the circumstances in which action may be taken;

The circumstances in which actions may be taken is described in Rules and Annex II (Default rules).

b) who may take those actions;

Authorised clearing and settlement specialist according to the internal rules and procedures of the Depository.

c) the scope of the actions which may be taken, including the treatment of both proprietary and customer positions, funds and assets;

Please see above. The Depository does not differentiate between customer and proprietary transactions. Only difference is that transfer orders may have different priority levels (see the response under Q.13.1.2 e) above).

d) the mechanisms to address an FMI's obligations to non-defaulting participants; and

Please see above.

e) where direct relationships exist with participants' customers, the mechanisms to help address the defaulting participant's obligations to its customers?

Estonian Settlement System

In case the status of an Account Operator to the Estonian Settlement System is revoked (e.g. upon commencement of insolvency proceedings), the Depository organises the transfer of the right to administer securities accounts opened through the insolvent Account Operator in the Estonian Settlement System to other account operators holding System Participant status in the Estonian Settlement System. Administration rights are transferred by a resolution of the Supervisory Council of the registrar which has to provide the time of the transfer of administration rights and other conditions and circumstances necessary to organise the transfer of administration rights so as to ensure that holders of securities accounts have the opportunity to enter into agreements for the use of their securities accounts through a new account operator. (§ 36 (2) – (5) of the ECRS Act).

Latvian Settlement System

Upon the request of the Depository, the Account Operator has to transfer the bookkeeping of the securities to the Depository if it is necessary to protect the interests of the Account Operators clients or the Account Operator has not transferred the securities bookkeeping to another Account Operator which is a Participant to the Latvian Settlement System within the term set by the Depository.

Lithuanian Settlement System

In case the status of the Account Operator to Lithuanian Settlement System has been revoked, the Depository stops operations in respect of this Account Operator (except for the operations related to the transfer of securities accounting to other Account Operators) and the Account Operator has to forfeit the right to manage personal financial instruments accounts. The entries made by such an Account Operator personal financial instruments accounts after the revoking of the Account Operator's status are invalid.

If the client terminates the agreement with the Account Operator on safe custody of his securities, the Depository organises the transfer of the right to administer securities accounts opened through the insolvent Account Operator in the Lithuanian Settlement System (i) to other Account Operator holding System Participant status in the Lithuanian Settlement System designated by the client or (ii), in case the client fails to designate such Account Operator, to the Issuer Agent. In case it is not possible to transfer the right to administer the securities account to the Issuer Agent (e.g. the agreement between the Issuer and the Account Operator is terminated), the Issuer within the same day has to (i) conclude an agreement with another Account Operator regarding the administration of the Issuer's securities accounts for the respective Securities Issue or (ii), in case the Issuer fails to do so, the Issuer has to provide the Depository with all the information regarding such securities accounts (*Articles 68(2)(2) and 87(5) of the Law on Markets in Financial Instruments*).

Key consideration 4: An FMI should involve its participants and other stakeholders in the testing and review of the FMI's default procedures, including any close-out procedures. Such testing and review should be conducted at least annually or following material changes to the rules and procedures to ensure that they are practical and effective.

Q.13.4.1: *How does the FMI engage with its participants and other relevant stakeholders in the testing and review of its participant default procedures? How frequently does it conduct such tests and reviews? How are these tests results used? To what extent are the results shared with the board, risk committee and relevant authorities?*

In compliance with Article 41(3) of the CSDR the Depository will undertake with its participants and other relevant stakeholders periodic testing and review of its default procedures to ensure that they are practical and effective. According to the Rules the participant has to participate in all the tests reasonably requested by the Depository.

The Depository considers introducing regular testing, with frequency at least once per year, of realistic default scenarios and procedures. Those tests will be focused on simulating realistic stress situations, including among others default of one or more major trading members.

Outcome of tests will be shared without delay with the Management Board, chief risk officer, compliance and internal control function and to the Supervisory Council. In case of any relevant findings, outcome of the tests will also be shared with the relevant user committee. Outcome of tests will also be shared with the relevant authorities or made available during annual review (to be arranged at least on an annual basis pursuant to Article 22 (1) of the CSDR).

Q.13.4.2: *What range of potential participant default scenarios and procedures do these tests cover? To what extent does the FMI test the implementation of the resolution regime for its participants?*

All realistic participant default scenarios and associated procedures will be covered to ensure that tests produce maximum benefit to the Depository and its stakeholders.

Under the article 22 (3) of the CSDR competent authority shall ensure that an adequate resolution plan is established and maintained for each CSD so as to ensure continuity of at least its core functions, having regard to the size, systemic importance, nature, scale and complexity of the activities of the CSD concerned and any relevant resolution plan established in accordance with Directive 2014/59/EU. The Depository is going to integrate relevant parts of the resolution regime to the testing in close consultation with FCMC.

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Principle 15: General business risk

An FMI should identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that it can continue operations and services as a going concern if those losses materialise. Further, liquid net assets should at all times be sufficient to ensure a recovery or orderly wind-down of critical operations and services.

This principle should be reviewed in the context of Principle 3 on the framework for the comprehensive management of risks, Principle 21 on efficiency and effectiveness, and other principles, as appropriate.

Key consideration 1: An FMI should have robust management and control systems to identify, monitor, and manage general business risks, including losses from poor execution of business strategy, negative cash flows, or unexpected and excessively large operating expenses.

Q.15.1.1: *How does the FMI identify its general business risks? What general business risks has the FMI identified?*

The Depository's risk management framework is based on Enterprise Risk Management (ERM) approach as explained under principle 3 and 17.

That includes regular assessment of all risks in terms of probability and impact of any occurrence, as well as action plans to mitigate the risks. Comprehensive risk self-assessment is conducted at least annually under the coordination of Nasdaq Group Risk Management function. Such self-assessment includes among others the assessment of commercial risks. Below main business risks have been identified by so far:

- > Vulnerability of Baltic market and Baltic region as whole due to factors like small market, not enough products, low liquidity and limited number of investors;
- > Loss of revenues because of local and European economic situation;
- > Growing and soon introduced (by CSD Regulation) opening of EU competition within the market of CSD services;
- > Risks stemming from the price control of the Ministry of Finance (see § 23 (1¹) of the ECSR Act that requires prior approval of service fees by the MoF) with regard to Estonian Securities Settlement System.

Q.15.1.2: *How does the FMI monitor and manage its general business risks on an on-going basis? Does the FMI's business risk assessment consider the potential effects on its cash flow and (in the case of a privately operated FMI) capital?*

Regular review and monitoring of Depository's financial performance and economic indicators by the Management Board and Supervisory Council is the main risk management tool. Risk assessment considers among other things effects on cash flow and capital.

Key consideration 2: An FMI should hold liquid net assets funded by equity (such as common stock, disclosed reserves, or other retained earnings) so that it can continue operations and services as a going concern if it incurs general business losses. The amount of liquid net assets funded by equity an FMI should hold should be determined by its general business risk profile and the length of time required to achieve a recovery or orderly wind-down, as appropriate, of its critical operations and services if such action is taken.

Q.15.2.1: *Does the FMI hold liquid net assets funded by equity so that it can continue operations and services as a going concern if it incurs general business losses?*

Under Article 47 of the CSDR the Depository has to maintain capital, retained earnings and reserves that are proportional to the risks stemming from the activities of the CSD. It shall be at all times sufficient to:

- (i) ensure that the Depository is adequately protected against operational, legal, custody, investment and business risks so that the Depository can continue to provide services as a going concern;
- (ii) ensure an orderly winding-down or restructuring of the Depository's activities over an appropriate time span of at least six months under a range of stress scenarios.

The capital, earnings and reserves should be sufficient to absorb potential losses arising from the Depository's activities. The Depository does not have other special-purpose financial resources.

Depository shall also be subject to supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on certain prudential requirements for central securities depositories and designated credit institutions offering banking-type ancillary services (pending for adoption).

Furthermore, under Article 22(2) of the CSDR the Depository will be under the requirement to submit to the competent authority an adequate recovery plan to ensure continuity of its critical operations.

Q.15.2.2: *How does the FMI calculate the amount of liquid net assets funded by equity to cover its general business risks? How does the FMI determine the length of time and associated operating costs of achieving a recovery or orderly wind-down of critical operations and services?*

Please see response to Q.15.2.1 – Depository will be subject to detailed prudential requirements under the CSDR framework.

Key consideration 3: An FMI should maintain a viable recovery or orderly wind-down plan and should hold sufficient liquid net assets funded by equity to implement this plan. At a minimum, an FMI should hold liquid net assets funded by equity equal to at least six months of current operating expenses. These assets are in addition to resources held to cover participant defaults or other risks covered under the financial resources principles. However, equity held under international risk-based capital standards can be included where relevant and appropriate to avoid duplicate capital requirements.

Recovery or orderly wind-down plan

Q.15.3.1: *Has the FMI developed a plan to achieve a recovery or orderly wind-down, as appropriate? If so, what does this plan take into consideration (for example, the operational, technological and legal requirements for participants to establish and move to an alternative arrangement)?*

No, this is in the action plan for 2017 as finalisation of this plan is strongly dependent on final legally binding version of the RTS on prudential requirements. As stated in level 1 of the CSDR, capital, retained earnings and reserves need to be sufficient to ensure an orderly winding-down or restructuring of the Depository's activities over an appropriate time span of at least six months under a range of stress scenarios. Plan shall be finalised without delay following the publication of RTS on prudential requirements.

Resources

Q.15.3.2: *What amount of liquid net assets funded by equity is the FMI holding for purposes of implementing this plan? How does the FMI determine whether this amount is sufficient for such implementation? Is this amount at a minimum equal to six months of the FMI's current operating expenses?*

No, this is in the action plan for 2017 as finalisation of this plan is strongly dependent on final legally binding version of the RTS on prudential requirements. As stated in level 1 of the CSDR, capital, retained earnings and reserves need to be sufficient to ensure an orderly winding-down or restructuring of the Depository's activities over an appropriate time span of at least six months under a range of stress scenarios. Plan shall be finalised without delay following the publication of RTS on prudential requirements.

Q.15.3.3: *How are the resources designated to cover business risks and losses separated from resources designated to cover participant defaults or other risks covered under the financial resources principles?*

As stated in level 1 of the CSDR and will be more specifically mandated in RTS on CSD's prudential requirements, capital, retained earnings and reserves need to be sufficient to ensure that the Depository is adequately protected against operational, legal, custody, investment and business risks so that the Depository can continue to provide services as a going concern.

Q.15.3.4: *Does the FMI include equity held under international risk-based capital standards to cover general business risks?*

Depository shall be bound by CSDR capital requirements, which include a requirement to have capital sufficient to manage also general business risks.

Key consideration 4: Assets held to cover general business risk should be of high quality and sufficiently liquid in order to allow the FMI to meet its current and projected operating expenses under a range of scenarios, including in adverse market conditions.

Q.15.4.1: *What is the composition of the FMI's liquid net assets funded by equity? How will the FMI convert these assets as needed into cash at little or no loss of value in adverse market conditions?*

Depository shall be bound by CSDR capital and prudential requirements and intends to comply with each of them.

Q.15.4.2: **How does the FMI regularly assess the quality and liquidity of its liquid net assets funded** by equity to meet its current and projected operating expenses under a range of scenarios, including in adverse market conditions?

Depository shall be bound by CSDR capital and prudential requirements and intends to comply with each of them.

Key consideration 5: An FMI should maintain a viable plan for raising additional equity should its equity fall close to or below the amount needed. This plan should be approved by the board of directors and updated regularly.

Q.15.5.1: *Has the FMI developed a plan to raise additional equity? What are the main features of the FMI's plan to raise additional equity should its equity fall close to or fall below the amount needed?*

There is written confirmation where Nasdaq AB, a parent company of Nasdaq Nordic Oy, confirms that to the best of its ability and taking into account its financial situation, it is prepared, to inject additional capital into the Depository in the amount necessary to secure a reliable and orderly functioning of the Depository in compliance with applicable prudential requirements and that Nasdaq AB is prepared to inject such capital as promptly as reasonably is required by using a combination of intra-group financing and capitalisation arrangements.

Final and formal plan is subject to finalisation in 2016,Q4 - 2017 (due to dependencies with final texts of RTSs). This will be based on the sequence of following logical steps that Depository would undergo in the event that results in urgent need for additional capital: Depository shall first request for additional capital from Nasdaq AB. Should Nasdaq AB refuse or be unable to contribute, Depository needs to request its participants to contribute additional equity. If participants refuse or fail to contribute, it will result in as orderly wind down of Depository as possible.

Q.15.5.2: *How frequently is the plan to raise additional equity reviewed and updated?*

The plan would be subject to annual review unless changes in the regulatory framework or other relevant circumstances trigger the need for extraordinary *ad hoc* review.

Q.15.5.3: *What is the role of the FMI's board (or equivalent) in reviewing and approving the FMI's plan to raise additional equity if needed?*

Depository's board would be required to ensure that the plan is viable and meets at minimum regulatory requirements and standards applicable to this kind of plans for CSDs.

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Principle 16: Custody and investment risks

An FMI should safeguard its own and its participants' assets and minimise the risk of loss on and delay in access to these assets. An FMI's investments should be in instruments with minimal credit, market, and liquidity risks.

This principle should be reviewed in the context of Principle 4 on credit risk, Principle 5 on collateral, Principle 7 on liquidity risk, and other principles, as appropriate.

Key consideration 1: An FMI should hold its own and its participants' assets at supervised and regulated entities that have robust accounting practices, safekeeping procedures, and internal controls that fully protect these assets.

Q.16.1.1: *If the FMI uses custodians, how does the FMI select its custodians? What are the specific selection criteria the FMI uses, including supervision and regulation of these entities? How does the FMI monitor the custodians' adherence to these criteria?*

The Depository holds its assets only with or via credit institution that has been approved in accordance with "Nasdaq Finance Policy".

Below is the extract of the relevant clauses of the said policy (please see underlined sections):

"9.1 Banks and Financial Counterparts

Group Treasury is responsible for selecting the external banks and financial counterparts and for maintaining relationship with banks and the capital markets.

The choice of banks shall be made from a long-term perspective and based on the bank's ability to provide financing, account structures, payments and other services to support Nasdaq.

Counterparty risk covers credit risks in investments or bank account balances as well as receivables that arise through derivatives contracts. Approved financial counterparties shall be evaluated using external credit ratings and/or internal analysis.

Group Treasurer will maintain a list of approved counterparties (Appendix 5) and is responsible for evaluating the bank relationships on a continuous basis.

Subsidiaries must have Group Treasury's approval to open bank accounts. Group Treasury is responsible to define bank and payment guidelines to which subsidiaries must adhere."

* Appendix 5 contains the names of highly rated credit institutions.

Q.16.1.2: *How does the FMI verify that these entities have robust accounting practices, safekeeping procedures, and internal controls that fully protect its and its participants' assets?*

The Depository has the following measures:

- (i) systems and controls are set out in the Nasdaq Financial Policy;
- (ii) each approved credit institution is subject to licencing and financial supervision in the relevant jurisdiction;
- (iii) assets (e.g. corporate action proceeds intended for the distribution to the account holders or corporate action proceeds accrued by the shareholders registered in the Initial Register are

held separately from the Depository's own assets and, where possible, with a cash account opened with the national central bank;

- (iv) full compliance CSDR and prudential requirements thereunder.

Key consideration 2: An FMI should have prompt access to its assets and the assets provided by participants, when required.

Q.16.2.1: *How has the FMI established that it has a sound legal basis to support enforcement of its interest or ownership rights in assets held in custody?*

By adherence to CSDR and its Group wide finance policy which provides careful selection of eligible counterparties (see response to Q. 16.1.1).

Latvian Settlement System

Please refer to information provided under Q.11.6.2 above regarding legal safeguards applicable to holding corporate action proceeds in safe custody on behalf of the shareholders registered in the Initial Register.

Q.16.2.2: *How does the FMI ensure that it has prompt access to its assets, including securities that are held with a custodian in another time zone or legal jurisdiction, in the event of participant default?*

By adherence to CSDR and Nasdaq Group wide finance policy which provides careful selection of eligible counterparties (see response to Q. 16.1.1).

Key consideration 3: An FMI should evaluate and understand its exposures to its custodian banks, taking into account the full scope of its relationships with each.

Q.16.3.1: *How does the FMI evaluate and understand its exposures to its custodian banks? In managing those exposures, how does it take into account the full scope of its relationship with each custodian bank? For instance, does the FMI use multiple custodians for the safekeeping of its assets to diversify exposure to any single custodian? How does the FMI monitor concentration of risk exposures to its custodian banks?*

By adherence to CSDR and Nasdaq Group wide finance policy which provides careful selection of eligible counterparties (see response to Q. 16.1.1).

Key consideration 4: An FMI's investment strategy should be consistent with its overall risk-management strategy and fully disclosed to its participants, and investments should be secured by, or be claims on, high-quality obligors. These investments should allow for quick liquidation with little, if any, adverse price effect.

Investment strategy

Q.16.4.1: *How does the FMI ensure that its investment strategy is consistent with its overall risk management strategy? How and to whom does the FMI disclose its investment strategy?*

The Depository shall maintain always low risk investment strategy which is in full compliance with CSDR and Nasdaq Group wide finance policy.

Q.16.4.2: *How does the FMI ensure on an on-going basis that its investments are secured by, or are claims on, high-quality obligors?*

By maintaining full compliance with CSDR and Nasdaq Group wide finance policy.

Risk characteristics of investments

Q.16.4.3: *How does the FMI consider its overall exposure to an obligor in choosing investments? What investments are subject to limits to avoid concentration of credit risk exposures?*

By maintaining full compliance with CSDR and Nasdaq Group wide finance policy.

Q.16.4.4: *Does the FMI invest participant assets in the participants' own securities or those of its affiliates?*

Not applicable. The Depository does not invest participant assets.

Q.16.4.5: *How does the FMI ensure that its investments allow for quick liquidation with little, if any, adverse price effect?*

By maintaining full compliance with CSDR and its Group wide finance policy.

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Principle 17: Operational risk

An FMI should identify the plausible sources of operational risk, both internal and external, and mitigate their impact through the use of appropriate systems, policies, procedures, and controls. Systems should be designed to ensure a high degree of security and operational reliability and should have adequate, scalable capacity. Business continuity management should aim for timely recovery of operations and fulfilment of the FMI's obligations, including in the event of a wide-scale or major disruption.

This principle should be reviewed in the context of Principle 20 on FMI links, Principle 21 on efficiency and effectiveness, Principle 22 on communication standards and procedures, and other principles, as appropriate.

Key consideration 1: An FMI should establish a robust operational risk-management framework with appropriate systems, policies, procedures, and controls to identify, monitor, and manage operational risks.

Identification of operational risk

Q.17.1.1: *What are the FMI's policies and processes for identifying the plausible sources of operational risks? How do the FMI's processes identify plausible sources of operational risks, whether these risks arise from internal sources (for example, the arrangements of the system itself, including human resources), from the FMI's participants or from external sources?*

The Depository has a risk management structure in place through the Nasdaq Enterprise Risk Management Framework. In accordance with Nasdaq risk management policy, risk self-assessment (RSA) is conducted annually and the management periodically reviews the results/targets. All types of risks are identified, probability and impact of each risk is assigned and the action plan to mitigate risks is developed during the RSA process.

Q.17.1.2: *What sources of operational risks has the FMI identified? What single points of failure in its operations has the FMI identified?*

The sources of operational risks identified by the Depository are:

- (i) Technology
- (ii) Legal environment
- (iii) Delivery
- (iv) Human related
- (v) Project
- (vi) Hazard
- (vii) Crime
- (viii) Environment

Single point of failures, as identified, have been mitigated with appropriate action plan (purpose, action, responsibility, due date) and are described in the Business Contingency Plan.

Management of operational risk

Q.17.1.3: *How does the FMI monitor and manage the identified operational risks? Where are these systems, policies, procedures and controls documented?*

Management and key personnel at all levels and areas are actively involved in periodic risk assessment reviews. The work is performed in following steps:

- (i) Identification
- (ii) Description (including category and type)
- (iii) Assessment (impact, probability)
- (iv) Management strategy (action plan, responsibilities, due date)
- (v) Identification of current controls
- (vi) Distribution of documents to participants, comments

Risk management systems, policies, procedures and controls are properly documented and are being kept on internal network, where authorized employee can access them.

Policies, processes and controls

Q.17.1.4: *What policies, processes and controls does the FMI employ that are designed to ensure that operational procedures are implemented appropriately? To what extent do the FMI's systems, policies, processes and controls take into consideration relevant international, national and industry-level operational risk management standards?*

Comprehensive set of policies, procedures and controls apply to the operations and IT security of the Depository given that it belongs to Nasdaq Group. These include regular security awareness trainings and extensive list of local as well as the following global (applicable in all parts of the Nasdaq Group) policies, guidelines and standards:

- > Enterprise Risk Management Guidelines
- > Rules of procedure for ordering and carrying out internal IT developments
- > Business continuity plan of the Depository (subject to finalisation)
- > Usage Policy Regarding Freeware and Internet Services
- > Global Nasdaq Information Security Policy
- > Global Nasdaq Acceptable Use Policy (concerning IT equipment)
- > Global Data Classification Policy
- > Global Mobile Device Policy
- > Global Access Control Standard
- > Application Security Standard

- > Intrusion Detection & Prevention Standard
- > Logging and Monitoring Standard
- > Network Security Standard
- > Password Standard
- > Application Security Assessment Guidelines
- > Security Awareness Training Guideline

The goal is to work together as an organization to cultivate and promote strong security culture, best practices and behaviours that are necessary to protect Nasdaq programs, systems and applications.

Most of the policies, standards and documents are aligned with international standards (e.g. ISO 27002), are developed by Nasdaq and are therefore industry-oriented.

Q.17.1.5: *What are the FMI's human resources policies to hire, train and retain qualified personnel, and how do such policies mitigate the effects of high rates of personnel turnover or key-person risk? How do the FMI's human resources and risk management policies address fraud prevention?*

Each year, Information Security and Corporate Operations require all Nasdaq employees to complete a web-based "Security Awareness Training" course. The purpose of the course is to inform and educate our global staff about best practices for keeping our information and physical property secure. Fraud prevention is embedded in the corporate policy framework.

Q.17.1.6: *How do the FMI's change management and project management policies and processes mitigate the risks that changes and major projects inadvertently affect the smooth functioning of the system?*

The change management and the project management processes are implemented to mitigate the risk that changes and major projects can reveal. Appropriate technical platforms are in place for analysis, testing, release management and incident management. If substantial hardware or software changes are planned in a system, the implications for the security of the system as a whole are examined. All changes to IT components, software or configuration data is planned, tested, approved and documented. If risks cannot be ruled out, especially as regards availability, a fall-back solution is planned and criteria established as to when this should be implemented.

Key consideration 2: An FMI's board of directors should clearly define the roles and responsibilities for addressing operational risk and should endorse the FMI's operational risk-management framework. Systems, operational policies, procedures, and controls should be reviewed, audited, and tested periodically and after significant changes.

Roles, responsibilities and framework

Q.17.2.1: *How has the board of directors defined the key roles and responsibilities for operational risk management?*

Personnel are responsible to comply with all the implemented security requirements to manage operational risks. Designated positions are responsible for operational risk management process compliance to the Chief Executives and the Supervisory Council. The policies are communicated to personnel, IT products, services, systems, and networks are evaluated and potential non-compliances and associated risks and potential impacts are identified. Department Heads and Product or Service owners are responsible for providing input for operational risk management in the implementation of their products or services. IT related personnel are providing input for operational risk management for the range of data, systems, networks, and applications that they manage.

Q.17.2.2: *Does the FMI's board explicitly review and endorse the FMI's operational risk management framework? How frequently does the board review and endorse the FMI's operational risk management framework?*

The risk management process is governed through the Enterprise Risk Management Framework of the Nasdaq Group. The process is supported by detailed guidelines on how to identify, assess, manage and control risks. All relevant observations and proposals considering operational risk management framework made during the annual review, can be reported to the Nasdaq Group and are taken into account for the following reviews.

Review, audit and testing

Q.17.2.3: *How does the FMI review, audit and test its systems, policies, procedures and controls, including its operational risk management arrangements with participants? How frequently does the FMI conduct these reviews, audits and tests with participants?*

The Internal Audit function of the Nasdaq Group is responsible for making independent reviews of the adequacy of operational risk controls, reporting to the Nasdaq Group Audit Committee. The board of directors of Nasdaq Group appoints the members of the Audit Committee. An annually approved Charter governs internal Audit.

On at least twice per year basis Depository conducts so called connectivity tests with all stakeholders (including participants and cooperating CSDs).

Q.17.2.4: *To what extent, where relevant, is the FMI's operational risk management framework subject to external audit?*

Depository's operational risk management framework and systems is subject to independent audits. The frequency of these audits shall be based on a documented risk assessment but it shall be no less than every two years pursuant to CSDR draft RTS (Article 73 "Audit and testing").

Key consideration 3: An FMI should have clearly defined operational reliability objectives and should have policies in place that are designed to achieve those objectives.

Q.17.3.1: *What are the FMI's operational reliability objectives, both qualitative and quantitative? Where and how are they documented?*

Reliability objectives are derived from the core business process requirements, from the requirements set by law and/or contracts, and are based on the analysis of consequences of potential incidents. Availability, integrity and confidentiality aspects of every requirement is documented as separate analysis document and is used as an input defining specific measures and actions, in order to ensure adequate level of operational reliability.

Following are the key objectives of the Depository operations:

- a) meet regulatory requirements applicable to its operations, including the uptime requirement of its main production IT systems according to the following service level conditions:
 - (i) downtime does not exceed 2 hours in no more than six occasions per year and
 - (ii) average availability of the systems per annum is at least 99,5%.

- b) offer internationally accepted communication procedures, communication standards and wide range of measures and tools that help to prevent settlement fails;
- c) serve its main customer groups (issuers and participants) in a timely fashion (i.e. that correct and complete issuer applications and transfer orders are processed within applicable deadlines);
- d) have settlement failure rates for the securities Settlement Systems operated by the Depository below **0.5 per cent per year**.
- e) maintain its overall risk rating* at level A (i.e. low risk CSD) per Depository Review and Risk Evaluation Service, provided by Thomas Murray Data Services.

Q.17.3.2: *How do these objectives ensure a high degree of operational reliability?*

Based on operational reliability objectives and taking into account all business process related resources, the specific set of measures and actions is developed. All measures are covered by specific controls.

Q.17.3.3: *What are the policies in place that are designed to achieve the FMI's operational reliability objectives to ensure that the FMI takes appropriate action as needed?*

Information Security policy, Privacy standard, Security baseline standard, Incident response manual, ICT specific policies as well as other local and global policies, guidelines and standards referred to in response to Q.17.1.4.

Key consideration 4: An FMI should ensure that it has scalable capacity adequate to handle increasing stress volumes and to achieve its service-level objectives.

Q.17.4.1: *How does the FMI review, audit and test the scalability and adequacy of its capacity to handle, at a minimum, projected stress volumes? How frequently does the FMI conduct these reviews, audits and tests?*

The capacity requirements are defined for the key systems, technical solutions and interfaces. During the planning phase of the systems non-functional requirements increase of volumes is taken into account. During the implementation phase the systems have undergone thorough performance and capacity tests as part of the preproduction integration tests on the actual hardware and software configuration.

In order to make sure the requirements are met, tests are performed regularly (once a year) or after major architectural changes in systems or changes in services. The key systems performance levels are continuously monitored in order to identify areas of improvement, but also to see if the service levels needs to be adjusted.

Q.17.4.2: *How are situations where operational capacity is neared or exceeded addressed?*

Situations where operational capacity is neared or exceeded are considered as serious incidents and are managed in accordance with incident response manual. Services and actions are prioritized and the most critical services will be focused on in the first place. Future initiatives or changes are presented in due time, are thoroughly discussed and analysed for potential impact. The service infrastructure is scaled up if needed and adequate tests are being carried out.

Key consideration 5: An FMI should have comprehensive physical and information security policies that address all potential vulnerabilities and threats.

Physical security

Q.17.5.1: *What are the FMI's policies and processes, including change management and project management policies and processes, for addressing the plausible sources of physical vulnerabilities and threats on an on-going basis?*

The Depository's Threat and Vulnerability Management Process is in place to ensure that all appropriate defences are put in place before an incident occurs.

Q.17.5.2: *Do the FMI's policies, processes, controls and testing appropriately take into consideration relevant international, national and industry-level standards for physical security?*

Standards for physical protection of assets and staff are developed for each individual business location depending on sensitivity, scope and type of operation and are based on corporate directives from Nasdaq Group Risk Management. This includes routines for sectioned access control, fire prevention and detection, guard services, camera surveillance and handling of incoming mail and deliveries.

All Nasdaq-owned IT resources (e.g. computers, network components, etc.) will be managed through an asset management process.

Facilities housing Information Technology will provide an availability level that meets service level minimums for the IT systems housed within that facility. These facilities will provide basic physical access controls, electronic intrusion detection, and visual surveillance at the facility perimeter. Internal areas housing concentrations of IT Systems will be additionally secured, alarmed, and monitored to limit access and maintain operational control consistent with the intended use and secure operation of the IT systems.

Information security

Q.17.5.3: *What are the FMI's policies and processes, including change management and project management policies and processes, for addressing the plausible sources of information security vulnerabilities and threats on an ongoing basis?*

The following policies are among the most relevant in the context of change management and information security vulnerabilities:

- (i) Rules of procedure for ordering and carrying out internal IT developments;
- (ii) Intrusion Detection & Prevention Standard;
- (iii) Application Security Assessment Guidelines.

Intrusion Detection Standard is the one that establishes the security monitoring, surveillance, and Intrusion Detection requirements for Nasdaq Networks and Systems. Intrusion Detection System - system which monitors network or system traffic for unauthorized or malicious behaviour. Intrusion Detection will detect actual or highly probable intrusions into network components and systems, or excursions from normal network or system operation and report/alert these intrusions to operations personnel in real or near-real time. Intrusion Detection strategies may include any combination of network and host intrusion detection sensors and management consoles, log consolidation and analysis tools/systems, and traffic analysis tools/system; which will provide the combined capability for effective surveillance of Nasdaq Networks and Systems.

Q.17.5.4: *Do the FMI's policies, processes, controls and testing appropriately take into consideration relevant international, national and industry-level standards for information security?*

Information Security Policies and Standards are designed to maintain the confidentiality, integrity and availability of information and which applies to development, maintenance and production of systems within the Depository as well as to outsourcing partners and third party vendors. Detailed standards and procedures have also been established in a great variety of IT security related areas such as firewall management, Internet access, intrusion detection, password management, remote access etc. there is an extensive internal Information Security and Internal Audit team responsible for continuously auditing and verifying IT Security and compliance.

Key consideration 6: An FMI should have a business continuity plan that addresses events posing a significant risk of disrupting operations, including events that could cause a wide-scale or major disruption. The plan should incorporate the use of a secondary site and should be designed to ensure that critical information technology (IT) systems can resume operations within two hours following disruptive events. The plan should be designed to enable the FMI to complete settlement by the end of the day of the disruption, even in case of extreme circumstances. The FMI should regularly test these arrangements.

Objectives of business continuity plan

Q.17.6.1: *How and to what extent does the FMI's business continuity plan reflect objectives, policies and procedures that allow for the rapid recovery and timely resumption of critical operations following a wide-scale or major disruption?*

A Business Continuity plan has been established, describing how to achieve continuity of the vital processes in the event of disruption of services. The critical business operations and corresponding resources are prioritized, organized and managed in order to fulfil obligations towards customers, partners, regulators and other stakeholders. Incident response procedures have been developed and are tested regularly with different scenarios and compositions. Technical back-up site is available, alternative communication channels are in place for data and telecommunication services. Employees can be given secure access to IT services outside of the office premises if necessary through firewalls using personal access codes and physical tokens.

Design of business continuity plan

Q.17.6.2: *How and to what extent is the FMI's business continuity plan designed to enable critical IT systems to resume operations within two hours following disruptive events, and to enable the FMI to facilitate or complete settlement by the end of the day even in extreme circumstances?*

Settlement is the time-critical process and in general restoration time must be up to 2 hours. Depending on the specifics of the incident, the Depository will reserve the possibility for extending the workday set forth in its Rules as follows:

“If the services provided by the Depository in connection with its Settlement System are interrupted for any reason, including as a result of a software error, telecommunications outage, unavailability of T2S services or Default Event of the Participant(s), the Depository shall use all reasonable efforts to minimise the duration of any interruption of the functioning of CSD System for the Participants and shall be entitled to apply the following contingency measures:

(i) changing the schedule for data processing and settlement activities, including temporary suspension of such activities, extraordinary extension of the working time of the Settlement System(s) and postponing of the Settlement Dates of affected Transfer Orders;

(ii) temporary restriction of access to the Settlement System or certain functionalities thereof;

(iii) forwarding Transfer Orders and other instructions issued for performing CSD activities of the Depository through alternative communication channels and, if necessary, manual processing of Transfer Orders and instructions so forwarded; and

(iv) other measures foreseen in the recovery plan of the Depository notified to the Participants or respective System Participants of the affected Settlement System."

Q.17.6.3: *How is the contingency plan designed to ensure that the status of all transactions can be identified in a timely manner, at the time of the disruption; and if there is a possibility of data loss, what are the procedures to deal with such loss (for example, reconciliation with participants or third parties)?*

If operations cannot be performed through GUI or the transaction volume does not allow the Account Operator manual entry, the Account Operator must send the respective file corresponding to the structure established by the Depository in a digitally signed and encrypted format by using alternative channels – e.g. e-mail.

Q.17.6.4: *How do the FMI's crisis management procedures address the need for effective communications internally and with key external stakeholders and authorities?*

It will be notified the external stakeholders and key persons of the special circumstances according to the internal communications plan. There are different levels (management, clients, partners) and communication channels (web, e-mail, phone). The following provisions have been also included to the Rules of the Depository:

"The Depository shall notify the affected Participants about the following regarding any material interruption at the earliest opportunity:

- (i) summarised description of the malfunction causing the interruption;
- (ii) any measure it has taken or shall take to limit the adverse consequences of such interruption and the predicted duration of such interruption; and
- (iii) where possible, other information, recommendations and instructions necessary for restoring the regular functioning of the affected Settlement System."

Secondary site

Q.17.6.5: *How does the FMI's business continuity plan incorporate the use of a secondary site (including ensuring that the secondary site has sufficient resources, capabilities, functionalities and appropriate staffing arrangements)? To what extent is the secondary site located a sufficient geographic distance from the primary site such that it has a distinct risk profile?*

The Depository's business continuity plan incorporates the use of secondary site. Sufficient resources cover all critical processes.

Q.17.6.6: *Has the FMI considered alternative arrangements (such as manual, paper-based procedures or other alternatives) to allow the processing of time-critical transactions in extreme circumstances?*

It has been considered and has been put in place as an alternative solution for time-critical transactions (e.g. physical mobile data medium). During the breakdown the partner has the possibility to send the respective file corresponding to the structure in a digitally signed and encrypted format.

Review and testing

Q.17.6.7: *How are the FMI's business continuity and contingency arrangements reviewed and tested, including with respect to scenarios related to wide-scale and major disruptions? How frequently are these arrangements reviewed and tested?*

The Depository foresees regular tests of Business Continuity Plans twice a year, during which a realistic incident will be simulated and application of the business continuity plan will be tested. Information collected during the course of testing will be used for updating the business continuity plan.

Participants are obliged to participate in testing according to the Rules of the Depository:

"Upon the request of the Depository within reasonable time before the commencement of testing the System Participant shall be obliged to participate in the testing of the recovery plan of the relevant Settlement System."

Q.17.6.8: *How does the review and testing of the FMI's business continuity and contingency arrangements involve the FMI's participants, critical service providers and linked FMIs as relevant? How frequently are the FMI's participants, critical service providers and linked FMIs involved in the review and testing?*

The Depository foresees regular tests of Business Continuity Plans twice a year, during which a realistic incident will be simulated and application of the business continuity plan will be tested. Information collected during the course of testing will be used for updating the business continuity plan. The FMI's participants, critical service providers and linked FMIs involved as appropriate.

Participants (*general term that includes all types of participants*) are obliged to participate in testing according to the Rules of the Depository (please refer to the information provided under Q. 17.6.7).

Key consideration 7: An FMI should identify, monitor, and manage the risks that key participants, other FMIs, and service and utility providers might pose to its operations. In addition, an FMI should identify, monitor, and manage the risks its operations might pose to other FMIs.

Risks to the FMI's own operations

Q.17.7.1: *What risks has the FMI identified to its operations arising from its key participants, other FMIs, and service and utility providers? How and to what extent does the FMI monitor and manage these risks?*

The Depository has outsourced parts of the IT responsibilities to external service providers, including parts of information systems hosting, development and support. All critical aspects are ascertained and external service providers are subject to supervision and audit as internal counterparts. External service providers and market participants are involved in Business Continuity Plans and meeting the requirements is regularly tested in order to fulfil the obligations towards customers, regulators and other key stakeholders.

The specific set of measures and actions is developed to cover risks and threats deriving from outsourcing. All measures are covered by adequate controls and audited regularly.

Q.17.7.2: *If the FMI has outsourced services critical to its operations, how and to what extent does the FMI ensure that the operations of a critical service provider meet the same reliability and contingency requirements they would need to meet if they were provided internally?*

Processes and systems have been verified by third parties. In addition there is an extensive internal Information Security and Internal Audit team responsible for continuously auditing and verifying IT Security and compliance.

There are contractual relationship between FMI and the critical service provider and the same reliability and contingency requirements are applied as they were provided internally.

Risks posed to other FMIs

Q.17.7.3: *How and to what extent does the FMI identify, monitor and mitigate the risks it may pose to another FMI?*

The Depository will notify the key participants of the special circumstances (new functionality, changes) according to the communication plan. Impact analysis are made and presented.

Q.17.7.4: *To what extent does the FMI coordinate its business continuity arrangements with those of other interdependent FMIs?*

The Depository will notify the key participants of the special circumstances according to the communication plan. Regular tests of Business Continuity Plans take place twice a year. Over the market tests will be organized after the significant changes/releases.

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Principle 18: Access and participation requirements

An FMI should have objective, risk-based, and publicly disclosed participation, criteria for which permit fair and open access.

In reviewing this principle, it should be noted that FMIs are subject to the constraints of local laws and policies of the jurisdiction in which the FMI operates, and those laws may prohibit or require the inclusion of certain categories of financial institutions. This principle should be reviewed in the context of Principle 19 on tiered participation arrangements, Principle 21 on efficiency and effectiveness, and other principles, as appropriate.

Key consideration 1: An FMI should allow for fair and open access to its services, including by direct and, where relevant, indirect participants and other FMIs, based on reasonable risk-related participation requirements.

Participation criteria and requirements

Q.18.1.1: *What are the FMI's criteria and requirements for participation (such as operational, financial and legal requirements)?*

Types of participants and general participation criteria

According to the Rules the Participant of the Depository is a legal entity that has the right to participate in one or several Settlement Systems of the Depository with one or more of the following statuses:

- (i) an Account Operator;
- (ii) a Cash Agent;
- (iii) an Issuer Agent;
- (iv) a Fund Administrator; and
- (v) Foreign CSD as Investor CSD.

Under Section 3.1. of Chapter I of the Rules an applicant requesting the right of participation has to belong to one of the following categories of legal entities:

- (i) **credit institution** within the meaning of Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast), organised under the laws of an EU/EEA Member State or, in

case the applicant's home state is not within the EU/EEA Member State, is licensed to conduct investment business in its home state and is therein subject to satisfactory supervision equivalent to what follows from the Banking coordination directive and is authorised to provide credit institution's services in Estonia, Latvia or Lithuania and provides custody services in Estonia, Latvia or Lithuania;

- (ii) **investment firm** within the meaning of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments ("**MiFID**"), organised under the laws of an EU/EEA Member State or, in case the applicant's home state is not within the EU/EEA Member State, is licensed to conduct investment business in its home state and is therein subject to satisfactory supervision equivalent to what follows from MiFID and, where applicable, is authorised to provide custody services in Estonia, Latvia or Lithuania.
- (iii) **central securities depository** of an EU/EEA Member State;
- (iv) **national central bank** participating in the Eurosystem;
- (v) **central counterparty (CCP)** within the meaning of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories;
- (vi) **Baltic Stock Exchange and any other operator of a regulated market or multilateral trading facility** within the meaning of MiFiD which is authorised in the EU/EEA Member State and has a right to provide its services in Estonia, Latvia or Lithuania;
- (vii) **Republic of Estonia, Republic of Latvia, Republic of Lithuania or other Member State of the EU or EEA** (as may be represented by the State Treasury, the Ministry of Finance or other authorised institution) and its local municipalities or any other public law legal person exercising authority within administrative territorial unit.

Specific participation criteria

In addition to the general participation criteria, under the Rules the applicant requesting the right of participation has to establish all the necessary arrangements to meet all of the obligations as attributed to the requested status under these Rules and Contractual Documents of the Depository, including:

- (i) in case of **Account Operator** – the applicant has to be a participant of T2 Component System or have in place an agreement with Cash Agent necessary for cash settlement arrangements;
- (ii) in case of **Cash Agent** – the applicant has to be a participant of T2 Component System;
- (iii) in case of **Issuer Agent** or **Fund Administrator** – the applicant has in place all the necessary contractual arrangements with the Issuer for which the role of Issuer Agent or Fund Administrator is applied for and shall be subject to all the admission criteria applicable to Account Operator.

The admission criteria and provisions on participation set out in the Rules apply to **EU/EEA Member State** (as may be represented by the State Treasury, the Ministry of Finance or other authorised institution) and its local municipalities or any other public law legal person exercising authority within administrative territorial unit and **national central banks participating in the Eurosystem** to the extent it is possible to apply these provisions to such entities having regard to their status and functions. In case of necessity the Depository may establish admission criteria and grounds for suspension and termination of access of these entities to the Depository or its services that derogate

from the provisions in the Rules.

Furthermore, the entities requesting the right of participation as of date of their admission should be able to comply with the participants' obligations set out in the Rules, including the obligation to:

- (i) comply with the Rules and Contractual Documents of the Depository, applicable laws, and observe good practice of the financial sector considering Participant's type(s), participation in the Settlement System(s) and activities for which it has applied or subscribed for, and to that effect maintain, among others, at all times operational capacity, financial resources, legal powers, risk-management expertise, compliance, operational and technical arrangements that are adequate to prevent the occurrence of risk for the investors, Depository, other Participants and the Issuer;
- (ii) considering Participant's type(s), participation in the Settlement System(s) and activities for which it has applied or subscribed for, ensure a connection(s) to the CSD System or , other IT systems or platforms (including T2S Platform in case of DCP) that meet(s) at all times the IT security and other technical requirements established by the Depository;
- (iii) ensure that, by means of appropriate administrative, technical and IT security measures information communicated to the Depository by the Participant and information available from the Depository or its Settlement Systems to the Participant, including information recorded with regard to securities accounts, is protected against unauthorised access and processing, including use, destruction or alteration;
- (iv) verify correctness and compliance with applicable legal and regulatory requirements of information and instructions communicated to the Depository;
- (v) have proper credit and liquidity management arrangements and other systems and controls in place.

Legal basis

Account Operator is the main participant type of the Depository. The Account Operator must comply with the provisions of CSDR in respect of CSD's participants and applicable national law requirements.

Q.18.1.2: *How do these criteria and requirements allow for fair and open access to the FMI's services, including by direct and, where relevant, indirect participants and other FMIs, based on reasonable risk-related participation requirements?*

Direct participants

The Depository's participation criteria are simple, transparent objective and non-discriminatory ensuring fair and open access to the Depository having due regard to risks to financial stability and the orderliness of markets in Estonia, Latvia and Lithuania (*Article 33(1) of the CSDR*). The participation is essentially available, among others, to any entity that is authorised to provide custody services or credit institution's services in Estonia, Latvia or/and Lithuania. The Depository, however, can deny access to a participant based on a comprehensive assessment of risks as may be provided in the CSDR technical standards (*Article 33(3) of the CSDR*).

Indirect participants

Payment Bank in T2S that is not a Cash Agent (i.e. credit institution established in Eurozone country other than Estonia, Latvia or Lithuania that is not a System Participant but is set up in T2S by a foreign CSD) could be classified as an indirect participant of Settlement Systems. Under the Rules the Participants may use DCAs of any Payment Bank in T2S in order to settle the cash leg in T2S provided that such Payment Banks have complied with the Estonian, Latvian or Lithuanian regulatory

requirements (e.g. passporting of the licence of a credit institution established in the Eurozone Member State to Estonia, Latvia or Lithuania) and T2S requirements. Such Payment Banks do not have contractual relationship with the Depository. Nevertheless, the Depository will maintain a link in T2S between DCA of a Payment Bank and an Operational Account of account holder.

Access to trade repositories

Q.18.1.3: *For a TR, how do the terms of access for use of its services help ensure that competition and innovation in post-trade processing are not impaired? How are these terms designed to support interconnectivity with other FMIs and service providers, where requested?*

Not applicable.

Key consideration 2: An FMI's participation requirements should be justified in terms of the safety and efficiency of the FMI and the markets it serves, be tailored to and commensurate with the FMI's specific risks, and be publicly disclosed. Subject to maintaining acceptable risk control standards, an FMI should endeavour to set requirements that have the least-restrictive impact on access that circumstances permit.

Justification and rationale of participation criteria

Q.18.2.1: *How are the participation requirements for the FMI justified in terms of the safety and efficiency of the FMI and its role in the markets it serves, and tailored to and commensurate with the FMI's specific risks?*

Design of the Settlement System and the services the participants provide to their clients through the Settlement System necessitates that the participants, depending on the participant type and status, are authorised to provide custody services or/and credit institution's services in Estonia, Latvian or Lithuania. Together with the increased need for Settlement System's financial stability this justifies the approach whereby financial institutions subject to financial supervision, primarily authorised credit institutions and investment firms, may become participants of the Depository.

The requirement that the applicant seeking to apply for the status of an Account Operator has to be a participant of T2 Component System or should have an agreement with a Cash Agent is necessitated by the need to ensure cash settlement in CSD System and/or T2S.

Q.18.2.2: *Are there participation requirements that are not risk-based but required by law or regulation? If so, what are these requirements?*

The participation requirements provided in the law referred to in response under Q.18.1.1 above are mainly risk-based or required to ensure smooth operation of the Settlement Systems and compliance with the applicable regulations.

Q.18.2.3: *Are all classes of participants subject to the same access criteria? If not, what is the rationale for the different criteria (for example, size or type of activity, additional requirements for participants that act on behalf of third parties, and additional requirements for participants that are non-regulated entities)?*

Yes, the main classes of participants are subject to the same general set of access criteria. Some variations apply to specific types of participants which are necessary to provide certain services to their clients (e.g. Cash Agents need to be a participant to T2 Component System in order to process cash transfers in CeBM).

However, the following exceptions apply:

- (i) the admission criteria and provisions on participation set out in the Rules apply to EU/EEA Member State (as may be represented by the State Treasury, the Ministry of Finance or other authorised institution) and its local municipalities or any other public law legal person exercising authority within administrative territorial unit and national central banks participating in the Eurosystem to the extent it is possible to apply these provisions to such entities having regard to their status and functions. In case of necessity the Depository may establish admission criteria and grounds for suspension and termination of access of these entities to the Depository or its services that derogate from the provisions provided in the Rules.
- (ii) the Depository's agreement with a Foreign CSD as Investor CSD which has requested access to the services of the Depositor may provide exemptions or additional requirements in order to access the Settlement Systems operated by the Depository via a CSD link arrangement.

Least restrictive access

Q.18.2.4: *How are the access restrictions and requirements reviewed to ensure that they have the least restrictive access that circumstances permit, consistent with maintaining acceptable risk controls? How frequently is this review conducted?*

There is no schedule for regular review of access criteria. Current system represents the requirements set in Article 33 of the CSDR and ensures a fair and open access to the Depository having due regard to financial stability and orderliness of the markets. The Depository welcomes suggestions from regulators, prospective and existing participants, and is committed to conduct due evaluation upon receiving suggestions regarding the access criteria. Furthermore, the User Committee of each Settlement System has the right to advise the Supervisory Council of the Depository on the criteria for admission of participants to the respective Settlement System.

Disclosure of criteria

Q.18.2.5: *How are participation criteria, including restrictions in participation, publicly disclosed?*

All sources containing participation criteria, including restrictions in participation, will be publicly available in compliance with Article 33(1) of the CSDR.

Key consideration 3: An FMI should monitor compliance with its participation requirements on an on-going basis and have clearly defined and publicly disclosed procedures for facilitating the suspension and orderly exit of a participant that breaches, or no longer meets, the participation requirements.

Monitoring compliance

Q.18.3.1: *How does the FMI monitor its participants' on-going compliance with the access criteria? How are the FMI's policies designed to ensure that the information it uses to monitor compliance with participation criteria is timely and accurate?*

The Depository monitors compliance of the participants with the requirements for the settlement operations and settlement discipline throughout the business day. Events that may represent material misconduct are referred to a legal counsel who initiates formal proceedings if necessary.

Furthermore, under the Rules the participants are *inter alia* under an obligation:

- (i) to notify any change in the information provided by it to the Depository as part of its Participant application which is material for the assessment of the compliance of the Participant with the admission conditions;
- (ii) to promptly notify the Depository of any and all circumstances that may cause a situation where a Participant is not, due to its solvency, change in legal status, technical interruption or restrictions on its activity established against it, able to perform its obligations in connection with its participation in the Settlement System(s) of the Depository (Default Event); and
- (iii) to follow precepts issued and instructions given by the Depository, provide any information requested by the Depository and, where the applicable law or the Rules expressly provide, allow on-site inspections to be carried out by the Depository if any of the foregoing is necessary to ensure or verify Participant's compliance with the requirements provided in the Rules.

Please refer to response under Q.13.1.1 regarding notification of commencement of insolvency proceedings to the Depository.

Other aspects of participants' compliance with financial regulations (e.g. prudential requirements applicable to credit institutions) are supervised by the competent authorities.

Q.18.3.2: *What are the FMI's policies for conducting enhanced surveillance of, or imposing additional controls on, a participant whose risk profile deteriorates?*

Under Article 7(9) of the CSDR and the CSDR technical standards the Depository reports to the competent authorities information of participants that fail consistently and systematically to deliver securities on ISD, in consultation with such authorities may suspend such participant and discloses the identity of the suspended participant to the public. The participant has the opportunity to submit observations before such a decision is taken. Please see provisions provided in the Rules (section 3.6).

Furthermore, risk-profile based tools are implemented by the operators of the Baltic Stock Exchanges that has the authority to impose *inter alia* settlement limits (member's or their client trades cannot exceed the value of the limit) on its members whose risk profile increases.

Suspension and orderly exit

Q.18.3.3: *What are the FMI's procedures for managing the suspension and orderly exit of a participant that breaches, or no longer meets, the participation requirements?*

The procedure for suspending and terminating the participant status are provided in the Rules and mandatory provisions of the law applicable to the respective participant.

Suspension

Under the Rules and to the extent permitted by applicable law, the Depository may at any time suspend the access of a Participant to all or part of the services and functionalities, with effect from such date and time as the Depository may specify:

- (i) if the Participant fails to comply with any of the requirements and admission criteria provided in the Rules or, in the reasonable opinion of the Depository, such failure is likely to occur;
- (ii) if the Participant is in breach of any material provisions of the Rules or, in the reasonable opinion of the Depository, any such breach is likely to occur;
- (iii) if the Participant is in breach of any provisions of the Rules and fails to remedy such breach within the time reasonably allocated to it by the Depository;

- (iv) if the outcome of consultations with relevant FSA carried out under Article 7(9) of the CSDR supports suspension of the Participant because of consistent and systematic settlement fails;
- (v) upon the occurrence of a Default Event other than an Insolvency Event affecting such Participant;
- (vi) if, in the reasonable opinion of the Depository, circumstances have arisen which represent a threat to the security, integrity or reputation of the Depository or the Settlement Systems of the Depository; or
- (vii) upon an order of the competent authority affecting the Participant's capacity or ability to transfer title to securities or exercise any right arising from such securities held by it with the Depository or serve the holders of securities accounts.

Under the Rules and to the extent permitted by the applicable Law, the Depository shall suspend the access of a Participant to all or part of the services and functionalities, with effect from such date and time as the Depository may specify having regard, where applicable, to the decision of the FSA or the relevant Central Bank:

- (i) upon the occurrence of an Insolvency Event, unless otherwise instructed by the appointed receiver, administrator, trustee or similar person;
- (ii) if the license required for the Participant to conduct its business which directly relates to the business for which the Participant is using the services provided by the Depository is suspended, in whole or in part, by the relevant FSA;
- (iii) if the Participant no longer has effective contractual arrangements in place enabling the Participant to have a Cash Account linked to respective securities account(s), including upon a decision of the relevant Central Bank to block or close the Cash Account linked to the respective securities accounts.

Subject to applicable mandatory provision of law, if any, any suspension continues for so long as the Depository considers appropriate and ends on such date and on such conditions as the Depository shall determine. The Depository informs the Participant at the latest when the suspension becomes effective, as to which services and functionalities the suspension relates.

The provisions of the Rules, so far as relevant, shall continue to apply to the Participant during any suspension.

In case of the **Estonian Settlement System**, general procedure for the suspension of the account operator's status is also provided in § 35 ECRS Act. The relevant Sections of the Rules comply with the statutory framework.

Termination

Under the Rules and to the extent permitted by applicable law, the Depository may at any time unilaterally terminate the participation agreement(s) with a Participant, for all or part of the services and functionalities, with effect from such date and time as the Depository may specify, upon any of the circumstances referred to in the Rules.

Any Participant may unilaterally terminate its contractual relationship with the Depository by giving the Depository at least 60 calendar days' notice thereof.

In case of the **Estonian Settlement System**, general procedure for the revocation and the waiver of the account operator's status is also provided in §§ 36 and 37 of the ECRS Act, respectively. The relevant Sections of the Rules comply with this statutory framework.

Consequences of suspension and termination

Under the Rules and where a Participant's contractual relationship with the Depository is suspended or terminated (whether by the Depository or at the Participant's initiative), such Participant and the Depository take all necessary steps to minimise the disruption to other clients that the suspension or termination could cause, and the Participant has to cooperate with the Depository in those matters that the Depository reasonably requires in relation to the suspension or termination.

The confidentiality and data protection obligations and dispute settlement procedure provided in the Rules survive the termination of the contractual relationship with the Participant.

Q.18.3.4: *How are the FMI's procedures for managing the suspension and orderly exit of a participant disclosed to the public?*

All sources containing suspension and termination (exit) of a participant are publicly available (please refer to 18.2.5 above regarding the links to the relevant sources).

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Principle 19: Tiered participation arrangements
An FMI should identify, monitor, and manage the material risks to the FMI arising from tiered participation arrangements.

This principle should be reviewed in the context of Principle 14 on segregation and portability, Principle 18 on access and participation requirements, and other principles, as appropriate.

Key consideration 1: An FMI should ensure that its rules, procedures, and agreements allow it to gather basic information about indirect participation in order to identify, monitor, and manage any material risks to the FMI arising from such tiered participation arrangements.

Tiered participation arrangements

Q.19.1.1: *Does the FMI have any tiered participation arrangements? If so, describe these arrangements.*

Rules of the Depository do not rule out arrangements which *de facto* may qualify as tiered participation arrangements.

Q.19.1.2: *How does the FMI gather basic information about indirect participation? Which information is collected and how frequently is it updated?*

Pursuant to the Rules the participant of the Depository shall provide to the Depository **any information**, including about Participants' clients and their settlement activities, that may be relevant for the Depository to identify, monitor, and manage any risks associated with tiered participation arrangements unless and insofar as mandatory law provides otherwise.

The Depository monitors the volume, dynamics and failure rates of settlement operations of its Participants for any anomalies. As soon as the such monitoring indicates anomalies and provides grounds to believe that these may be due to tiered participation arrangement(s) that may impose risks to the orderly functioning of any of Depository's Settlement System a request for additional information (not available from the CSD System or other sources accessible to the Depository) shall be provided to the Participant in question.

Risks to the FMI

Q.19.1.3: *How does the FMI evaluate its risks arising from these arrangements?*

The Depository evaluates the risk by constant monitoring of settlement operations and discipline. Primary participant has the primary responsibility for reacting to deterioration of settlement discipline from the tiered participant. The Depository considers any deterioration in settlement discipline problematic if this is likely to result in:

- (a) the value of settlement fails in the securities Settlement Systems operated by the Depository exceeding EUR 2.5 billion per year; and
- (b) the rate of settlement fails based on the number of settlement instructions, or based on the value of settlement instructions, for the securities Settlement Systems operated by the Depository is below 0.5 per cent per year.

Q.19.1.4: *What material risks to the FMI arising from tiered participation arrangements has the FMI identified? How has it mitigated these risks?*

Primary objective of the Depository is to ensure orderly functioning of its Settlement Systems. Deterioration of settlement discipline beyond certain pre-defined metrics would increase the risk that Settlement System(s) in question are not considered safe and sound which in turn may translate into loss of business.

Key consideration 2: An FMI should identify material dependencies between direct and indirect participants that might affect the FMI.

Q.19.2.1: *How does the FMI identify material dependencies between direct and indirect participants that might affect the FMI?*

The Depository can identify **some of dependencies** (but not all) between direct (Account Operator) and indirect (major client) based on the design and functional logic of its operational model and account typology. For the identification of dependencies that the Depository itself cannot identify request(s) for additional information will follow on when needed basis.

Key consideration 3: An FMI should identify indirect participants responsible for a significant proportion of transactions processed by the FMI and indirect participants whose transaction volumes or values are large relative to the capacity of the direct participants through which they access the FMI in order to manage the risks arising from these transactions.

Q.19.3.1: *Has the FMI identified (a) the proportion of activity that each direct participant conducts on behalf of indirect participants in relation to the direct participants' capacity, (b) direct participants that act on behalf of a material number of indirect participants, (c) indirect participants responsible for a significant proportion of turnover in the system, and (d) indirect participants whose transaction volumes or values are large relative to the capacity of the direct participant through which they access the FMI to manage risks arising from these transactions?*

The Depository will be able to gather any of the above information taking into account the provisions of the Rules. According to the Rules the Participant shall provide to the Depository **any information**, including about Participants' clients and their settlement activities, that may be relevant for the Depository to identify, monitor, and manage any risks associated with tiered participation arrangements unless and insofar as mandatory law provides otherwise.

Q.19.3.2: *What risks to the FMI arise, and how does the FMI manage these risks arising from key indirect participants?*

Primary objective of the Depository is to ensure orderly functioning of its Settlement Systems. Deterioration of settlement discipline beyond certain pre-defined metrics would increase the risk that Settlement System(s) in question are not considered safe and sound which in turn may translate into loss of business.

Current statistics and allocation of volumes between direct and indirect participants allows us to conclude that no extra steps need to be taken at this stage. The Depository shall consider the imposition of *ad hoc* or automatic settlement limits, other restrictions or disciplinary measures that are available to the Depository under its Rules, CSDR or applicable law as soon as this proves to be necessary.

Key consideration 4: An FMI should regularly review risks arising from tiered participation arrangements and should take mitigating action when appropriate.

Q.19.4.1: *What are the FMI's policies for reviewing its rules and procedures in order to mitigate risks to the FMI arising from tiered participation? How frequently is this review conducted?*

The Depository evaluates the risk by constant monitoring of settlement operations and discipline. The Depository intends to make more detailed study at least once per year if results of its constant monitoring allow to conclude that there is one or more tiered participation arrangement where volume of settlement instructions is above 5% per annum.

Q.19.4.2: *What criteria does the FMI use to determine when mitigating actions are required? How does the FMI monitor and mitigate its risks?*

Material and systematic deterioration of settlement discipline due to reasons directly attributable to the tiered participation arrangement. The Depository shall consider the imposition of *ad hoc* or automatic settlement limits, other restrictions or disciplinary measures that are available to the Depository under its Rules, CSDR or applicable law as soon as this proves to be necessary.

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Principle 20: FMI links
 An FMI that establishes a link with one or more FMIs should identify, monitor, and manage link-related risks.

In reviewing this principle, it should be noted that the questions apply only to FMIs that have established links with one or more other FMIs. Additionally, the term CSD generally refers to a CSD that also operates an SSS. The use of this broader definition for CSD in this principle mirrors market convention in the discussion of FMI links. This principle should be reviewed in the context of Principle 8 on settlement finality, Principle 11 on CSDs, Principle 17 on operational risk, and other principles, as appropriate.

Key consideration 1: Before entering into a link arrangement and on an on-going basis once the link is established, an FMI should identify, monitor, and manage all potential sources of risk arising from the link arrangement. Link arrangements should be designed such that each FMI is able to observe the other principles in this report.]

Q.20.1.1: *What process is used to identify potential sources of risk (such as, legal, credit, liquidity, custody and operational risks) arising from prospective links? How does this affect the FMI's decision whether to establish the link?*

Depository has designed link-specific risk assessment questionnaire that is used both for prospective and existing links. Regular (annual basis for existing links) risk assessment procedure has been put in place to ensure that various risks, including those that may be due to elements of another jurisdiction, are at acceptable level for links that are operational.

Q.20.1.2: *What links have been established with other FMIs? How does the FMI identify, monitor and manage the risks arising from an established link on an on-going basis?*

Prior to merger of Baltic CSDs bilateral links between all Baltic CSDs were functional and supported cross-border settlement of FoP, DvP and stock exchange transactions. Given that the Depository is going to adopt a new operational model following the merger of Baltic CSDs (*and formation the Nasdaq CSD SE as a result of such merger*) these links will be discontinued, effective migration of the Depository to the T2S.

As a result the Depository is going to have the following links on the date of its migration to T2S:

- 1) Link with Clearstream Banking Luxembourg (CBL) where the Depository acts as an Investor CSD *via* its Latvian and Lithuanian Securities Settlement Systems;
- 2) Link with Polish Central Securities Depository (KDPW) where the Depository Acts as an Issuer CSD *via* its Estonian Securities Settlement System.

Please see response to Q.20.1.1 when it comes to identification, monitoring and management of risks of established links (*link-specific risk assessment questionnaire and annual risk assessment routine*).

Q.20.1.3: *How does the FMI ensure that link arrangements are designed so that it is able to remain observant of the other principles? How frequently is this analysis conducted?*

The Depository has designed link-specific risk assessment questionnaire that is used both for prospective and existing links. Annual risk assessment procedure has been put in place to ensure that various risks are at acceptable level and enable the Depository to maintain compliance with all relevant principles.

Key consideration 2: A link should have a well-founded legal basis, in all relevant jurisdictions, that supports its design and provides adequate protection to the FMIs involved in the link.

Q.20.2.1: *In which jurisdictions has the FMI established links? What are the relevant legal frameworks supporting the established links?*

As explained under Q.20.1.3 on the date of joining T2S the Depository will act as:

- 1) Investor CSD towards CBL in which case laws of Luxembourg and contractual arrangements with CBL provide relevant legal framework. In addition laws of Latvia and Lithuania are of relevance depending on whether the securities originating from CBL are transferred to and held in Depository's Latvian or Lithuanian Securities Settlement System;
- 2) Issuer CSD towards KDPW in which case Estonian laws are of primary relevance given that KDPW is accessing instruments from Depository's Estonian Securities Settlement System. Polish laws are of secondary relevance given that KDPW is Polish legal entity.

Q.20.2.2: *How does the FMI ensure that its links have a well-founded legal basis that support its design and provide it with adequate protection in all relevant jurisdictions? How does the FMI ensure that such protections are maintained over time?*

The Depository ensures that its links have a well-founded legal basis through thorough risk analysis that is conducted both with respect to prospective (prior to entering into link arrangement) and existing links.

Key consideration 3: Linked CSDs should measure, monitor, and manage the credit and liquidity risks arising from each other. Any credit extensions between CSDs should be covered fully with high-quality collateral and be subject to limits.

Q.20.3.1: *What processes are in place to measure, monitor and manage credit and liquidity risks arising from any established links?*

Regular risk assessment of links is the main tool and procedure. The design and operational model of the links listed under Q.20.1.2 does not expose the Depository to any credit or liquidity risk because the Depository extends no credit to any of the linked CSDs.

Q.20.3.2: *If a CSD extends credit to a linked CSD, what processes exist to ensure that credit extensions to the linked CSD are fully covered by high-quality collateral and that credit limits are appropriate?*

The Depository does not provide or extend any credit to linked CSDs.

Key consideration 4: Provisional transfers of securities between linked CSDs should be prohibited or, at a minimum, the retransfer of provisionally transferred securities should be prohibited prior to the transfer becoming final.

Q.20.4.1: *Are provisional transfers of securities allowed across the link? If so, what arrangements make provisional transfers necessary, and is the retransfer of these securities prohibited until the first transfer is final?*

None of the links listed under Q.20.1.2 involve provisional transfers. Transfers are made per issuer CSD model whereby investor CSD does its debits and credits following the confirmation of the issuer CSD about the irrevocable settlement of both cash (where relevant) and securities.

Key consideration 5: An investor CSD should only establish a link with an issuer CSD if the arrangement provides a high level of protection for the rights of the investor CSD's participants.

Q.20.5.1: *For any established link, how has the investor CSD determined that the rights of its participants have a high level of protection?*

Depository has conducted general evaluation of the issuer CSD's legal and operational framework and established that potential risks do not extend beyond tolerance limits.

Q.20.5.2: *How frequently is reconciliation of holdings conducted by the entities holding the securities in custody?*

On top of CSDR reconciliation requirements, applicable agreements provide daily reconciliation between each and every linked CSD.

Q.20.5.3: *How does the investor CSD provide a high-level of protection for the rights of its participants (including segregation and portability arrangements and asset protection provisions for omnibus accounts)?*

Depository as investor CSD has established link termination procedures aimed at achieving appropriate level of portability and asset protection.

Key consideration 6: An investor CSD that uses an intermediary to operate a link with an issuer CSD should measure, monitor, and manage the additional risks (including custody, credit, legal, and operational risks) arising from the use of the intermediary.

Q.20.6.1: *If the CSD uses an intermediary to operate a link, what are the criteria used by the CSD to select the intermediary or intermediaries? Are these criteria risk-based?*

Depository has no link arrangement involving the use of intermediary.

Q.20.6.2: *What are the respective liabilities of the two linked CSDs and the intermediaries?*

Depository has no link arrangement involving the use of intermediary.

Q.20.6.3: *What processes exist to measure, monitor and manage the risks arising from use of the intermediary?*

Depository has no link arrangement involving the use of intermediary.

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Principle 21: Efficiency and effectiveness

An FMI should be efficient and effective in meeting the requirements of its participants and the markets it serves.

This principle should be reviewed in the context of Principle 17 on operational risk, Principle 18 on access and participation requirements, Principle 22 on communication procedures and standards, and other principles, as appropriate.

Key consideration 1: An FMI should be designed to meet the needs of its participants and the markets it serves, in particular, with regard to choice of a clearing and settlement arrangement; operating structure; scope of products cleared, settled, or recorded; and use of technology and procedures.

Q.21.1.1: *How does the FMI determine whether its design (including its clearing and settlement arrangement, its operating structure, its delivery systems and technologies, and its individual services and products) is taking into account the needs of its participants and the markets it serves?*

Depository determines whether its design is taking into account the needs of its participants and the markets based on its ability to:

- a) meet regulatory requirements applicable to its operations, including the uptime requirement of its main production IT systems according to the service level conditions provided by CSDR and delegated legislation thereof.
- b) offer internationally accepted communication procedures, communication standards and wide range of measures and tools that help to prevent settlement fails;
- c) serve its main customer groups (issuers and participants) in a timely fashion (i.e. that correct and complete issuer applications and transfer orders are processed within applicable deadlines);
- d) with respect to settlement fails rate - to ensure that:
 - (i) the value of settlement fails in the securities settlement system operated by a the Depository does not exceed EUR 2.5 billion per year; and

- (ii) the rate of settlement fails based on the number of settlement instructions, or based on the value of settlement instructions, for the securities settlement system operated by the Depository is below 0.5 per cent per year
- e) maintain its overall risk rating* at level A (i.e. low risk CSD) per Depository Review and Risk Evaluation Service, provided by Thomas Murray Data Services.

* Rating scale

 AAA Extremely low risk

AA+ Very low risk

AA

AA-

A+ Low risk

A

A-

BBB Acceptable risk

BB Less than acceptable risk

B Quite high risk

CCC High risk

Q.21.1.2: *How does the FMI determine whether it is meeting the requirements and needs of its participants and other users and continues to meet those requirements as they change (for example, through the use of feedback mechanisms)?*

Mainly in the form of monitoring and following up on developments of metrics listed in response to Q.21.1.1 at least once a year.

Key consideration 2: An FMI should have clearly defined goals and objectives that are measurable and achievable, such as in the areas of minimum service levels, risk-management expectations, and business priorities.

Q.21.2.1: *What are the FMI's goals and objectives as far as the effectiveness of its operations is concerned?*

Please see metrics listed in response to Q.21.1.1.

Q.21.2.2: *How does the FMI ensure that it has clearly defined goals and objectives that are measurable and achievable?*

Please see metrics listed in response to Q.21.1.1.

Q.21.2.3: *To what extent have the goals and objectives been achieved? What mechanisms does the FMI have to measure and assess this?*

The first assessment following the merger of Baltic CSDs (and formation of the Nasdaq CSD SE) will be made within 12 months following the migration to T2S.

Key consideration 3: An FMI should have established mechanisms for the regular review of its efficiency and effectiveness.

Q.21.3.1: *What processes and metrics does the FMI use to evaluate its efficiency and effectiveness?*

Depository monitors and follows up on developments of metrics listed in response to Q.21.1.1 at least once a year.

Q.21.3.2: *How frequently does the FMI evaluate its efficiency and effectiveness?*

At least once a year by monitoring and following up on developments of metrics listed in response to Q.21.1.1.

PS	CSD	SSS	CCP	TR
•	•	•	•	•

Principle 22: Communication procedures and standards

An FMI should use, or at a minimum accommodate, relevant internationally accepted communication procedures and standards in order to facilitate efficient payment, clearing, settlement, and recording.

This principle should be reviewed in the context of Principle 17 on operational risk, Principle 21 on efficiency and effectiveness, and other principles, as appropriate.

Key consideration 1: An FMI should use, or at a minimum accommodate, internationally accepted communication procedures and standards.

Communication procedures

Q.22.1.1: *Does the FMI use an internationally accepted communications procedure and, if so, which one(s)? If not, how does the FMI accommodate internationally accepted communication procedures?*

A common CSD System is used for operation of Settlement Systems of the Depository, including for the record keeping, data processing and information exchange that is necessary to comply with T2S Framework Agreement, maintain Estonian Register of Securities and provide other CSD services. Functionality of CSD System shall be available to participants through special-purpose client application (CSD System GUI) and other communication channels provided in Operating Manual(s) and Technical Documentation of the Depository which include standardized communications protocol ISO 20022 over SWIFTNet or direct MQ interface.

Q.22.1.2: *If the FMI engages in cross-border operations, how do the FMI's operational procedures, processes and systems use or otherwise accommodate internationally accepted communication procedures for cross-border operations?*

Cross border operations are based on SWIFT communication and messaging standards.

Communication standards

Q.22.1.3: *Does the FMI use an internationally accepted communications standard and, if so, which one(s)? If not, how does the FMI accommodate internationally accepted communication standards?*

Yes, ISO 20022 is used as the main messaging standard.

Q.22.1.4: *If the FMI engages in cross-border operations, how do the FMI's operational procedures, processes and systems use or otherwise accommodate internationally accepted communication standards for cross-border operations?*

Yes, ISO 20022 is used as the main messaging standard. If requested by the requesting CSD also ISO 15022 can be supported until further notice.

Q.22.1.5: *If no international standard is used, how does the FMI accommodate systems that translate or convert message format and data from international standards into the domestic equivalent and vice versa?*

Not applicable.

PS	CSD	SSS	CCP	TR
•	•	•	•	•

Principle 23: Disclosure of rules, key procedures, and market data

An FMI should have clear and comprehensive rules and procedures and should provide sufficient information to enable participants to have an accurate understanding of the risks, fees, and other material costs they incur by participating in the FMI. All relevant rules and key procedures should be publicly disclosed.

In reviewing this principle, information should be disclosed to the extent that it would not risk prejudicing the security and integrity of the FMI or divulging commercially sensitive information. This principle should be reviewed in the context of Principle 8 on settlement finality, Principle 13 on participant default rules and procedures, Principle 24 on the disclosure of market data by trade repositories, and other principles, as appropriate.

Key consideration 1: An FMI should adopt clear and comprehensive rules and procedures that are fully disclosed to participants. Relevant rules and key procedures should also be publicly disclosed.

Rules and procedures

Q.23.1.1: *What documents comprise the FMI's rules and procedures? How are these documents disclosed to participants?*

Rules of Nasdaq CSD (or "**Rules**") which are composed of:

- (i) Chapter I which contains common provisions that apply to all Participants, Issuers and Settlement Systems;
- (ii) Chapter II which contains provisions that apply to Estonian Settlement System;
- (iii) Chapter III which contains provisions that apply to Latvian Settlement System;
- (iv) Chapter IV which contains provisions that apply to Lithuanian Settlement System;
- (v) Annexes (Chapters I to IV and Annex together are referred to as the ("Rules" or "Rulebook");
- (vi) any document to which these Rules refer to and which supplements these Rules, including Operating Manual, Price List, general Service Description, individual Service Description, Corporate Action Service Description, User Guide, Technical Documentation or any agreement regarding the use of CSD services provided by the Depository. Each of these documents is deemed to be incorporated in, and constitutes an integral part of the Rules of the Depository.

Publicly available Chapters of the Rules will be disclosed to participants and general public at the official website of the Depository.

Q.23.1.2: *How does the FMI determine that its rules and procedures are clear and comprehensive?*

We consider that inter alia the following demonstrates and proves that rules, procedures and contracts of the Depository are clear and comprehensive:

1. extensive consultations with all the relevant stakeholders, including the Participants, were carried out prior to the adoption of the rules;
2. the fact that relevant sections of the Depository's Rules are subject to prior consultations with the respective competent authority;
3. the fact that the Estonian Settlement System is subject to oversight by Eesti Pank, the Latvian Settlement System is subject to oversight by the Bank of Latvia and the Lithuanian Settlement System is subject to oversight by the Bank of Lithuania;
4. the fact that rules, contracts and key procedures are subject to mandatory review and approval of the in-house representative of the Office of General Counsel (Nasdaq's cross-organisational unit of international legal counsels and compliance experts); and
5. the fact that Office of General Counsel has been assigned the responsibility for keeping rules and contracts up to date and consistent with relevant laws.

Disclosure

Q.23.1.3: *What information do the FMI's rules and procedures contain on the procedures it will follow in non-routine, though foreseeable, events?*

The information about the procedures that the Depository will follow in non-routine (foreseeable) events is provided in the section 2.7 of the Rules.

Q.23.1.4: *How and to whom does the FMI disclose the processes it follows for changing its rules and procedures?*

Provisions covering the amendment procedure of Rules are available to the public as these are included in its publicly available Chapter of Rules – please see section 2.3 of the Rules:

Q.23.1.5: *How does the FMI disclose relevant rules and key procedures to the public?*

Publicly available Chapters of the Rules will be disclosed to participants and general public at the official website of the Depository.

Key consideration 2: An FMI should disclose clear descriptions of the system's design and operations, as well as the FMI's and participants' rights and obligations, so that participants can assess the risks they would incur by participating in the FMI.

Q.23.2.1: *What documents comprise information about the system's design and operations? How and to whom does the FMI disclose the system's design and operations?*

Rules of the Depository provide a very precise information about systems's design and operations. In particular Service Description(s) (General Service Description and Service Description about Corporate

Actions) latest version of which have been made available to the Participants through dedicated section of Depository's website.

Q.23.2.2: *How and to whom does the FMI disclose the degree of discretion it can exercise over key decisions that directly affect the operation of the system?*

Decree of discretion is provided in the CSDR, delegated legislation thereunder, applicable national laws and Rules of the Depository. All of the aforementioned sources are or will be available to the general public.

Q.23.2.3: *What information does the FMI provide to its participants about their rights, obligations and risks incurred through participation in the FMI?*

Rules of the Depository as well as statutory legislation are available to public without any exceptions. Thus Depository has provided to participants all the information what is needed to shape complete understanding of their rights, obligations and risks.

Key consideration 3: An FMI should provide all necessary and appropriate documentation and training to facilitate participants' understanding of the FMI's rules and procedures and the risks they face from participating in the FMI.

Q.23.3.1: *How does the FMI facilitate its participants' understanding of the FMI's rules, procedures and the risks associated with participating?*

Depository facilitates its participants' understanding of the FMI's rules, procedures and the risks associated with participating by disclosures referred to under Q.23.2.1.

Q.23.3.2: *Is there evidence that the means described above enable participants' understanding of the FMI's rules, procedures and the risks they face from participating in the FMI?*

Below evidence supports that the means described above enable participants' understanding of the Depository's (or its legal predecessors') rules, procedures and the risks they face from participating in Settlement Systems operated by Baltic CSDs:

- > Low settlement failure rate;
- > low rate of legal disputes;
- > CSD Rating (by Thomas Murray): A+ .

Q.23.3.3: *In the event that the FMI identifies a participant whose behaviour demonstrates a lack of understanding of the FMI's rules, procedures and the risks of participation, what remedial actions are taken by the FMI?*

Please see responses to Q.18.3.3 describing suspension and revocation procedures.

Key consideration 4: An FMI should publicly disclose its fees at the level of individual services it offers as well as its policies on any available discounts. The FMI should provide clear descriptions of priced services for comparability purposes.

Q.23.4.1: *Does the FMI publicly disclose its fees at the level of its individual services and policies on any available discounts? How is this information disclosed?*

Yes, the Depository is going publicly discloses its fees at the level of individual services at the official website of the Depository.

Q.23.4.2: *How does the FMI notify participants and the public, on a timely basis, of changes to services and fees?*

Please refer to the response provided under Q.23.1.4.

Q.23.4.3: *Does the FMI provide a description of its priced services? Do these descriptions allow for comparison across similar FMIs?*

Yes, in the Price List. To the best of our understanding pricing model of the Depository is not unique which allows comparison(s) with similar FMIs.

Q.23.4.4: *Does the FMI disclose information on its technology and communication procedures, or any other factors that affect the costs of operating the FMI?*

Yes, to the regulators that under the applicable laws have the authority to request information qualifying as commercial secret.

Key consideration 5: An FMI should complete regularly and disclose publicly responses to the CPSS-IOSCO disclosure framework for financial market infrastructures. An FMI also should, at a minimum, disclose basic data on transaction volumes and values.

Q.23.5.1: *When did the FMI last complete the CPSS-IOSCO Disclosure framework for financial market infrastructures? How frequently is it updated? Is it updated following material changes to the FMI and its environment and, at a minimum, every two years?*

Baltic CSDs have previously disclosed their responses on their respective websites. As for the Depository, it intends to disclose most of its responses to present questionnaire on its official website.

Q.23.5.2: *What quantitative information does the FMI disclose to the public? How often is this information updated?*

Depository intends to comply with every information disclosure obligation required under the CSDR or local national laws.

Q.23.5.3: *What other information does the FMI disclose to the public?*

Please visit the official websites of the Baltic CSDs..

Q.23.5.4: *How does the FMI disclose this information to the public? In which language(s) are the disclosures provided?*

Please visit the official websites of the Baltic CSDs.

Annex I

NASDAQ CSD LEGAL STRUCTURE AS OF SEPTEMBER 2017



NASDAQ CSD GOVERNANCE STRUCTURE

AS OF SEPTEMBER 2017

