

# Deposit Guarantee Fund

## Annual Report 1999

Financial year: 1 January 1999 – 31 December 1999

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<b>Auditor:</b>	KPMG Estonia

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## Preface, Signatures

The director general of the Deposit Guarantee Fund has prepared the activity report and the annual financial statements for 1999.

The annual report of the Deposit Guarantee Fund (pp. 1-18) consists of the activity report, the annual financial statements, and the auditor's report.

The annual report was approved by the supervisory board of the Deposit Guarantee Fund on \_\_\_\_\_ 2000.

	Name	Date	Signature
Director General	Madis Kallion	.....	.....
<b><u>Supervisory Board:</u></b>			
Chairman	Helo Meigas	.....	.....
Member	Siim Kallas	.....	.....
Member	Viktor Hütt	.....	.....
Member	Jaan Pöör	.....	.....
Member	Tiit Sinissaar	.....	.....

# Activity Report

## **Purpose and Management**

The Deposit Guarantee Fund (hereinafter “the Fund”) is a public legal person founded on the basis of law. The purpose of its activities is to guarantee the deposits placed with credit institutions by depositors in the event of the insolvency of the credit institutions by arranging compensation of deposits consistent with law. The Fund is managed by a five-member supervisory board and director general.

During the financial year, two members of the supervisory board were replaced. The Government of the Republic recalled Mart Opmann, a former Minister of Finance, and appointed Siim Kallas as a new Member of the board. The management board of the Estonian Banking Association recalled Viktor Hütt in connection with his resignation as director general of the Association and appointed Katrin Talihärm, the new director general, as his replacement. The supervisory board of the Fund elected Katrin Talihärm the new vice chairman of the Board.

At the end of the financial year the Fund had four employees. Payroll expenses amounted to EEK 896,528 including EEK 465,757 of remuneration paid to director general and members of the supervisory board.

## **Compensation of Deposits**

The Fund continued compensation of deposits to customers of EVEA Bank and ERA Bank through Hansabank and Union Bank of Estonia. For the customers of EVEA Bank and ERA Bank the legally prescribed term for payment of compensation expired on 4 January 1999 and 8 January 1999, respectively. Compensation that had not been paid by those dates was deposited with Hansabank and Union Bank of Estonia based on a resolution taken by the supervisory board.

According to law, to receive unpaid compensation a depositor may file a claim against the Fund. For satisfaction of claims and payment of compensation, the Fund opened special accounts with Hansabank and Union Bank of Estonia. Through these accounts, depositors of EVEA Bank and ERA Bank were paid unpaid compensation from 1 March to 31 May 1999. Satisfaction of claims continued from 1 October 1999.

Compensation paid during the year amounted to EEK 10,581,800: 830 depositors of EVEA Bank received EEK 4,148,996 and 1,068 depositors of ERA Bank received EEK 6,432,804. At the end of the year, unpaid compensation amounted to EEK 3,171,360.

## **The Fund's Activities in Bankruptcy Proceedings**

EVEA Bank was declared bankrupt on 5 February 1999 and ERA Bank was declared bankrupt on 7 June 1999. The Fund has the right to claim from EVEA Bank and ERA Bank the compensation that has been paid to their depositors.

In bankruptcy proceedings against EVEA Bank, the Fund filed a claim of EEK 98,260,457, which was fully recognised at the claim defence meeting in May 1999.

The Fund's claim against ERA Bank amounts to EEK 37,647,567. The amount was defended at the creditor's meeting in March 2000.

As a major creditor, the Fund actively participated in the selection and initiation of the creditors committee of ERA Bank and the renewal of the creditors committee of EVEA Bank. The Fund also participated in rearranging the work of the creditors committee of EVEA Bank.

## **Investment of the Fund's Assets**

In February 1999, the Fund repaid the EEK 75 borrowed from Hansabank with a loan obtained from Merita Bank. The new loan was considerably more favourable and it had a state guarantee. In November, the Fund also fully repaid the loan taken from Merita Bank.

After settlement of the loan liabilities, the Fund had unrestricted funds of EEK 21 million, which were placed with the Bank of Estonia. The Fund concluded an agreement with the Bank of Estonia with respect to investment of the funds consistent with legal restrictions. The agreement will remain effective until the general principles governing the investment of the Fund's assets have taken effect.

The supervisory board approved, in principle, the principles governing the investment of the Fund's assets. The board approved the final wording of the document in February 2000. The principles will take effect on 1 July 2000.

## **Increase in the Extent of Compensation for Guaranteed Deposits**

Consistent with the *Deposit Guarantee Fund Act*, from 1 October 1998 the extent of compensation for guaranteed deposits was EEK 20,000. By the year 2010 it will increase to EUR 20,000. According to the resolution adopted by the supervisory board, from 1 January 2000 the extent of compensation for guaranteed deposits is EEK 40,000. The extent of compensation is going to increase as follows: 1 January 2004 – EEK 100,000, 1 January 2007 – EEK 200,000, 1 January 2010 – EEK 313,000.

## **Basic Directions for 2000**

The Fund will continue fulfilling its legal obligations.

Compensation will be paid to those depositors of EVEA Bank and ERA Bank, who have claimed unpaid compensation. As one of the largest creditors, the Fund will remain actively involved in the bankruptcy proceedings of EVEA Bank and ERA Bank.

From 1 July 2000, the Fund's assets should be invested according to a new procedure. By that time, all documents required for the implementation of the new investment principles should be complete and approved by the supervisory board.

We will continue analysing the *Deposit Guarantee Fund Act* and developing its amendment proposals in co-operation with the Bank of Estonia and the Estonian Banking Association.

Development of implementation acts, which regulate submission by credit institutions of information required by the Fund, will continue in co-operation with the Estonian Banking Association.

We intend to open our home page in the Internet and will continue international co-operation with institutions involved in guaranteeing deposits.

## Annual Financial Statements

### Deposit Guarantee Fund

#### Balance Sheet

31 December 1999

In Estonian kroons

	Note	31.12.1999	31.12.1998
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and bank	2	3,722,985	7,067,137
Short-term investments	3	21,016,252	
Accrued income			
Interest receivable	4	118,450	150,923
Total		118,450	150,923
Prepaid expenses	5	2,924	1,628
<b>Total current assets</b>		<b>24,860,611</b>	<b>7,219,688</b>
<b>Non-current assets</b>			
Tangible assets	6	407,280	390,380
Accumulated depreciation	6	(151,087)	(25,992)
Total		256,193	364,388
Intangible assets	6	8,090	14,150
<b>Total non-current assets</b>		<b>264,283</b>	<b>378,538</b>
<b>TOTAL ASSETS</b>		<b>25,124,894</b>	<b>7,598,226</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Current liabilities</b>			
Short-term loans from credit institutions		-	74,905,018
Accrued expenses			
Interest payable		-	760,847
Other payables	7	4,048	-
Total		4,048	760,847
<b>Total current liabilities</b>		<b>4,048</b>	<b>75,665,865</b>
<b>Fund (equity) at end of financial year</b>		<b>25,120,846</b>	<b>(68,067,639)</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>25,124,894</b>	<b>7,598,226</b>

Deposit Guarantee Fund

**Statement of Changes in Fund**

1999

In Estonian kroons

	Note	1999	1998
<b>Fund (equity) at beginning of financial year</b>		<b>(68,067,639)</b>	-
Received from credit institutions	8	108,185,948	54,646,741
Compensation paid to depositors	9	10,581,800	120,810,948
<b>Total interest income</b>	14	<b>180,849</b>	<b>153,053</b>
Interest earned on deposits		180,849	153,053
<b>Total interest expense</b>	13	<b>2,523,117</b>	<b>1,036,045</b>
Interest paid on loans		2,523,117	1,036,045
<b>Net interest income</b>		<b>(2,342,268)</b>	<b>(882,992)</b>
Investment income	14	70,956	-
<b>Net investment income</b>		<b>70,956</b>	-
Other operating expenses	12	46,510	
<b>Total administrative expenses</b>		<b>2,097,841</b>	<b>1,020,440</b>
Salaries	10	896,528	199,512
Social taxes	10	295,856	65,838
Other administrative expenses	11	774,302	728,088
Depreciation and value adjustments	6	131,155	27,002
<b>Net result of the fund</b>		<b>93,188,485</b>	<b>(68,067,639)</b>
<b>Fund (equity) at end of financial year</b>		<b>25,120,846</b>	<b>(68,067,639)</b>

Deposit Guarantee Fund

**Cash Flow Statement**

31 December 1999

In Estonian kroons

	<b>1999</b>	<b>1998</b>
<b>Cash flows from operating activity</b>		
Payments received from credit institutions	108,185,948	54,646,741
Compensation paid to depositors	(10,581,800)	(120,810,948)
Operating and personnel expenses	(1,963,925)	(995,066)
Interest paid	(3,283,965)	(275,198)
<b>Net cash used in operating activity</b>	<b>92,356,258</b>	<b>(67,434,471)</b>
<b>Cash flows from investing activities</b>		
Non-current assets acquired	(16,900)	(405,540)
Short-term investment in the Bank of Estonia	(21,016,252)	
Interest received	284,278	2,130
<b>Net cash used in investing activities</b>	<b>(20,748,874)</b>	<b>(403,410)</b>
<b>Cash flows from financing activities</b>		
Loans received	77,981,250	74,905,018
Loans repaid	(152,932,786)	-
<b>Net cash used in/received from financing activities</b>	<b>(74,951,536)</b>	<b>74,905,018</b>
<b>Net cash flows</b>	<b>(3,344,152)</b>	<b>7,067,137</b>
<b>Cash and cash equivalents at beginning of period</b>	<b>7,067,137</b>	<b>-</b>
<b>Cash and cash equivalents at end of period</b>	<b>3,722,985</b>	<b>7,067,137</b>

## Notes to the Annual Accounts

### **Note 1 Accounting Policies**

#### ***General Information***

The Deposit Guarantee Fund (hereinafter “the Fund”) is a public legal person without share capital founded under the *Deposit Guarantee Fund Act*, which entered into force on 23 May 1998. 1999 was the second financial year for the Fund.

The purpose of the Fund is to guarantee the deposits placed with credit institutions by depositors in the event of the insolvency of the credit institutions under the terms and in the extent provided by law.

Since the previous financial year was shorter than 12 months, the income and expenses for 1999 are not comparable to those of 1998.

#### ***Bases of Preparation***

The annual financial statements of the Deposit Guarantee Fund have been prepared in accordance with the *Deposit Guarantee Fund Act*, the *Estonian Accounting Act*, and generally accepted accounting principles.

#### ***Recognition of Foreign Currency Transactions***

Foreign currency transactions are accounted for using the Bank of Estonia exchange rate quoted at the date of the transaction. In the balance sheet, foreign currency receivables and payables are translated using the Bank of Estonia closing exchange rate. Revaluation gains and losses are reported in the statement of changes in fund and recognised as other operating income or other operating expenses.

#### ***Cash and bank***

To receive payments and make settlements, the Fund has a current account with a credit institution operating in Estonia as required by the *Deposit Guarantee Fund Act*. Payments received by the Fund have to be invested within three working days of their receipt in the account of the Fund using the procedure prescribed by law. The balance of the account shall not exceed the amount required for the continuous activity of the Fund.

The Fund has opened term deposits with two credit institutions. Compensation payable to the depositors of EVEA Bank and ERA Bank has been deposited there. To obtain unpaid compensation, depositors may file a claim against the Fund. To satisfy the claims, the Fund has opened special accounts with the same credit institutions. The Fund cannot use the amounts for any other purpose.

### ***Receipts***

The Fund's receipts include single payments made on the foundation of credit institutions, obligatory contributions from credit institutions, income from the investment of its assets, and other receipts. Single payments and obligatory contributions by credit institutions are reported in the statement of changes in fund as receipts from credit institutions on cash basis, other receipts are recorded on accrual basis.

Until 1 January 2002, obligatory quarterly contributions made by credit institutions are to equal 0.125% of the deposits taken by them. Obligatory contributions are calculated as of the end of the quarter and remitted to the Fund by the fifteenth of the second month of every quarter.

### ***Compensation paid to Depositors***

Compensation paid to depositors comprises the amount of deposits calculated consistent with the *Deposit Guarantee Fund Act* that has been paid to the depositors of EVEA Bank and ERA Bank. Compensation paid to depositors is recorded on cash basis.

### ***Off-balance Sheet Receivables***

When compensation has been paid to depositors, the right to claim from the credit institution to the extent of the compensation transfers to the Fund. The rights to claim are treated as off-balance sheet receivables because the recoverability of the receivables cannot be assessed with reasonable accuracy. If assets are received from a credit institution, they are reported as income.

### ***Off-balance Sheet Liabilities***

Compensation that has not been paid to depositors as of the balance sheet date but which has to be paid upon claim is reported as an off-balance sheet liability. Under the law, compensation has to be paid within three months of the date when the deposits became unavailable. Compensation that has not been paid within that term is deposited and the entitled persons have the right to file a claim against the Fund.

### ***Non-current Assets***

Assets whose acquisition cost exceeds EEK 5,000 and estimated useful life extends beyond one year are recorded as non-current assets. Immaterial assets whose acquisition cost is less than EEK 5,000 are expensed as of implementation.

Non-current assets are depreciated in line with their estimated useful lives using the straight-line method as follows:

Equipment and vehicles	30% per annum
Computer hardware	40% per annum
Buildings	5% per annum
Intangible assets	20% per annum

Depreciation commences from the month of implementation.

## Note 2 Cash and Bank

	<b>31.12.1999</b>	<b>31.12.1998</b>
Current account with Hansabank	552,754	88,042
Special account with Hansabank	376,440	3,321,236
Special account with Union Bank of Estonia	193,791	3,567,816
Term deposit with Hansabank	1,300,000	
Term deposit with Union Bank of Estonia	1,300,000	
Current account with the Bank of Estonia		90,043
<b>Total</b>	<b>3,722,985</b>	<b>7,067,137</b>

Special accounts are used for paying compensation to depositors.

## Note 3 Short-term Investments

	<b>31.12.1999</b>
Investment in the Bank of Estonia	21,016,252
<b>Total</b>	<b>21,016,252</b>

The Fund has concluded an agreement with the Bank of Estonia concerning the investment of the Fund's assets consistent with the restrictions outlined in the *Deposit Guarantee Fund Act* and the foreign currency management principles of the central bank. The Bank of Estonia guarantees the Fund's assets an average rate of return, which corresponds to the rate of return earned by the Bank of Estonia in investing similar funds of its own. The Fund has the right to withdraw the money with a two-day notice. The agreement remains in effect until general principles for investing the Fund's assets have been enacted.

## Note 4 Accrued Income

	<b>31.12.1999</b>	<b>31.12.1998</b>
Interest receivable on term deposit with Hansabank	1,787	
Interest receivable on term deposit with Union Bank of Estonia	61,178	
Interest receivable on investment in the Bank of Estonia	54,747	150,923
Interest receivable on special account with Union Bank of Estonia	738	
<b>Total</b>	<b>118,450</b>	<b>150,923</b>

The Bank of Estonia secures the investment of the Fund's assets the same average rate of return, which the central bank earns on the investment of foreign currency reserves.

### Note 5 Prepaid Expenses

	<b>31.12.1999</b>	<b>31.12.1998</b>
Prepayments to employees	1,317	279
Prepayments to suppliers	1,607	1,349
<b>Total</b>	<b>2,924</b>	<b>1,628</b>

### Note 6 Non-current Assets

	<b>31.12.1999</b>	<b>31.12.1998</b>
Computers	61,216	107,128
Car	149,680	221,536
Other non-current assets	45,297	35,724
Intangible assets	8,090	14,150
<b>Total non-current assets at net book value</b>	<b>264,283</b>	<b>378,538</b>

Non-current assets are carried at cost less accumulated depreciation. Intangible assets comprise a computer programme.

	Intangible assets	Computers and other	Car
<b>Acquisition cost</b>			
Balance as at 31.12.1998	15,160	150,880	239,500
Additions		16,900	
Balance as at 31.12.1999	15,160	167,780	239,500
<b>Accumulated depreciation</b>			
Balance as at 31.12.1998	1,010	8,028	17,964
Increase	6,060	53,239	71,856
Balance as at 31.12.1999	7,070	61,267	89,820
<b>Net book value as at 31.12.1999</b>	<b>8,090</b>	<b>106,513</b>	<b>149,680</b>

### Note 7 Accrued Expenses

	<b>31.12.1999</b>
Credit card expenses	2,425
Supplier payables	1,623
<b>Total</b>	<b>4,048</b>

## Note 8 Receipts from Credit Institutions

	<b>31.12.1999</b>	<b>31.12.1998</b>
Hansabank	66,034,180	29,934,747
Union Bank of Estonia	35,681,162	17,422,889
Optiva Bank	4,170,003	4,599,693
Estonian Credit Bank	1,977,565	1,140,040
Tallinn Business Bank	273,038	171,249
Preatoni Bank	50,000	
EVEA Bank		796,322
ERA Bank		581,801
<b>Total</b>	<b>108,185,948</b>	<b>54,646,741</b>

The receipt from Preatoni Bank is the payment, which is to be made to the Fund after the Supervisory Board of the Bank of Estonia has resolved to grant a credit institution an operating licence.

## Note 9 Compensation Paid to Depositors

	<b>31.12.1999</b>	<b>31.12.1998</b>
<b>Compensation has been paid to:</b>		
Depositors of EVEA Bank	4,148,996	91,678,763
Depositors of ERA Bank	6,432,804	29,132,185
<b>Total</b>	<b>10,581,800</b>	<b>120,810,948</b>

## Note 10 Personnel Expenses

	<b>31.12.1999</b>	<b>31.12.1998</b>
Salaries	896,528	199,512
inc. management and supervisory board	465,757	111,739
Social security	295,856	65,838
<b>Total</b>	<b>1,192,384</b>	<b>265,350</b>

At the end of 1999, the Fund had four employees and the supervisory board had five members.

### Note 11 Other Administrative Expenses

	<b>31.12.1999</b>	<b>31.12.1998</b>
Rental expenses	133,458	22,002
Transport, vehicle maintenance	71,963	36,129
Immaterial items	22,310	8,530
Information and communication expenses	230,279	79,845
Loan agreement fee	75,000	405,000
Other operating expenses	241,292	176,582
<b>Total</b>	<b>774,302</b>	<b>728,088</b>

### Note 12 Other Operating Expenses

	<b>31.12.1999</b>
Foreign exchange loss	46,510
<b>Total</b>	<b>46,510</b>

### Note 13 Interest Expense

	<b>31.12.1999</b>	<b>31.12.1998</b>
Interest paid on the loan taken from Hansabank	1,064,285	1,036,045
Interest paid on the loan taken from Merita Bank	1,458,832	
<b>Total</b>	<b>2,523,117</b>	<b>1,036,045</b>

The loan taken from Hansabank of EEK 77,905,036 was repaid in February 1999 with a loan taken from Merita Bank. The loan taken from Merita Bank of EEK 75,000,000 was taken in German marks and had a state guarantee. The loan was fully repaid in November 1999.

## Note 14 Income

	<b>31.12.1999</b>	<b>31.12.1998</b>
<b>Interest income</b>	<b>180,849</b>	<b>153,053</b>
Interest income on deposit with Hansabank	78,014	
Interest income on deposit with Union Bank of Estonia	80,768	
Interest income on current account with Hansabank	20,818	2,130
Interest income on special account with Hansabank	512	
Interest income on special account with Union Bank of Estonia	737	
Interest income on current account with the Bank of Estonia		150,923
<b>Investment income</b>	<b>70,956</b>	
Return on investment in the Bank of Estonia	70,956	
<b>Total income</b>	<b>251,805</b>	<b>153,053</b>

## Note 15 Off-balance Sheet Receivables

	<b>31.12.1999</b>
<b>Receivables from EVEA Bank</b>	<b>98,260,457</b>
Compensation of deposits	97,502,517
Completely unpaid contribution, III quarter of 1998	726,059
Partly unpaid contribution, II quarter of 1998	31,881
<b>Receivables from ERA Bank</b>	<b>37,647,567</b>
Compensation of deposits	37,059,649
Completely unpaid contribution, III quarter of 1998	488,556
Partly unpaid contribution, II quarter of 1998	99,362
<b>Total</b>	<b>135,908,024</b>

EVEA bank was declared bankrupt on 5 February 1999. The Fund's claim was fully recognised at the claim defence meeting in May 1999.

ERA Bank was declared bankrupt on 7 June 1999. The claim was defended at the creditors' meeting in March 2000.

## Note 16 Off-balance Sheet Liabilities

	<b>1999</b>	<b>1998</b>
<b>Deposits to be compensated</b>		
Depositors of EVEA Bank	5,825,694	97,361,960
Depositors of ERA Bank	7,927,466	36,893,832
<b>Total</b>	<b>13,753,160</b>	<b>134,255,792</b>
<b>Compensation paid</b>		
Depositors of EVEA Bank	4,148,996	91,678,764
Depositors of ERA Bank	6,432,804	29,132,184
<b>Total</b>	<b>10,581,800</b>	<b>120,810,948</b>
<b>Uncompensated deposits</b>	<b>31.12.1999</b>	<b>31.12.1998</b>
Depositors of EVEA Bank	1,676,698	5,683,196
Depositors of ERA Bank	1,494,662	7,761,648
<b>Total</b>	<b>3,171,360</b>	<b>13,444,844</b>

Unpaid compensation has been deposited with Hansabank and Union Bank of Estonia. To receive compensation for a guaranteed deposit, the depositor has the right to file a claim against the Fund. To satisfy the claims and pay compensation, the Fund has opened special accounts with Hansabank and Union Bank of Estonia.

## **AUDITOR'S REPORT TO THE SUPERVISORY BOARD OF THE DEPOSIT GUARANTEE FUND**

*(Translation from the Estonian language)*

We have audited the accompanying financial statements of the Deposit Guarantee Fund, comprising the balance sheet as of 31 December 1999, the related statement of changes in fund for the year then ended, and the notes to the financial statements. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Estonian Guidelines on Auditing. Those guidelines require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the financial position of the Deposit Guarantee Fund as of 31 December 1999, and of the results of its operations for the year then ended in accordance with the Estonian Accounting Act.

Tallinn, 25 May 2000

KPMG Estonia

*(signature)*

Taivo Epner  
*Authorised Public Accountant*