

Template for notifying the intended use of a systemic risk buffer (SRB)

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| 1. Notifying national authority and scope of the notification | |
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| 1.1 Name of the notifying authority | Financial Supervisory Authority of Iceland (FME) |
| 1.2 Type of measure intended (also for reviews of existing measures) | Maintain an existing SRB. The SRB was first introduced in Iceland on 1 April 2016. |
| 2. Description of the notified measure | |
| 2.1 Institutions covered by the intended SRB | <p>SRB will be applied to the following credit institutions on a consolidated basis:</p> <ol style="list-style-type: none"> 1) Arion banki hf. (LEI code: RIL4VBPDB0M7Z3KXSF19) 2) Íslandsbanki hf. (LEI code: 549300PZMFIQR79Q0T97) 3) Kvika banki hf. (LEI code: 254900WR3I1Z9NPC7D84) 4) Landsbankinn hf. (LEI code: 549300TLZPT6JELDWM92) 5) Sparisjóður Austurlands hf. (LEI code: 967600ZISRIPDC9ERJ93) 6) Sparisjóður Höfðhverfinga ses. (LEI code: 254900H6IYQMB9RAU056) 7) Sparisjóður Strandamanna ses. (LEI code: 9676003QL0SA69DLD253) 8) Sparisjóður Suður-Pingeyinga ses. (LEI code: 967600OER0PGHRKQTB65) |
| 2.2 Buffer rate (Article 133(11)(f) of the CRD) | <p>A buffer rate of 3% of RWA will continue to apply to systemically important institutions for the Icelandic economy (O-SIIs). These are Arion banki hf, Íslandsbanki hf and Landsbankinn hf.</p> <p>A phase-in buffer rate of 2% of RWA will continue to apply to other institutions covered by the measure. These are Kvika banki hf, Sparisjóður Austurlands hf, Sparisjóður Höfðhverfinga ses, Sparisjóður Strandamanna ses and Sparisjóður Suður-Pingeyinga ses. On 1 January 2020 the phase-in period will end and the buffer rate applied to these institutions will increase to 3% of RWA.</p> |

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| 2.3 Exposures covered by the SRB | The SRB applies to domestic exposures only. |
| 3. Timing of the measure | |
| 3.1 Timing of the Decision | 15 May 2018 |
| 3.2 Timing of the Publication | 15 May 2018 |
| 3.3 Disclosure | <p>Justification of the buffer was published when it was activated, see here: https://en.fme.is/media/news/en_Systemic-risk-buffer_final.pdf</p> <p>The justification for maintaining the buffer is still valid. All information on decisions and notification regarding capital buffers is available on FME's website, see here: https://en.fme.is/supervision/financial-stability/capital-buffers/</p> |
| 3.4 Timing of Application | 15 May 2018 |
| 3.5 Phasing in | The measure has been implemented in full for O-SII. For smaller institutions the buffer rate is currently 2% but will increase to 3% of RWA on 1 January 2020. |
| 3.6 Review/deactivation of the measure | The measure will be reviewed every other year and will therefore be in place at least until Q2 2020. The indicators used as part of the decision process are based on long term fluctuations in economic variables, e.g. GDP growth, private consumption, investments, imports/exports and inflation. These indicators will also be used to recalibrate or deactivate the measure. |
| 4. Reasons for the intended SRB | |
| 4.1 Description of the long-term non-cyclical systemic risk in your Member State (Article 133(11)a of the CRD) | <p>Iceland is a small open economy with its own currency, the Icelandic Krona (ISK), and is sensitive to developments in the global economy, especially in main trading countries. Iceland relies heavily on exports. Main exports include fish, aluminium and, more recently, tourism. Economic variables, e.g. GDP growth, private consumption, investments and imports/exports fluctuate more than in most other European countries. These fluctuations translate into a more uncertain economic environment with higher credit risk of banks. The entire financial sector is exposed to the elevated credit risk arising from the inherent structural vulnerabilities of the Icelandic economy.</p> |
| 4.2 Reasons why the dimension of the long-term non-cyclical systemic risk threatens the stability of the financial system in your Member State (Article 133(11)(b) of the CRD) | <p>The main weaknesses of the Icelandic economy can be explained by its small size, its currency and the reliance on a few important exports (fish, aluminium and tourism).</p> <p>Experience has shown that unexpected shocks can lead to a drastic increase in debt servicing problems in the non-financial sector with the potential to pose a serious solvency risk to banks.</p> <p>The credit institutions that the SRB is applied to are all vulnerable to the same risks. They must therefore maintain the SRB to bolster the</p> |

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| | resilience of the financial system as a whole. |
| 4.3 Indicators used for the activation of the measure | <ul style="list-style-type: none"> • The volatility of key economic performance indicators: Foreign exchange rates and GDP growth and underlying factors, like private consumption, exports and investments, fluctuate more in Iceland than in most other European economies leading to higher credit risk of banks. • Household indebtedness: Has been high in Iceland historically due to high ratio of home ownership. • The size and openness of the economy: Iceland is a small open economy. • The composition of exports: Iceland relies on a few export industries that are sensitive to world market conditions (fishing, aluminium and tourism) • Credit institutions exposures to a limited range of domestic based industries and consumer markets. |
| 4.4 Effectiveness and proportionality of the measure (Article 133(11)(c) of the CRD) | <p>The SRB aims to increase the resilience of the financial system in Iceland and in the medium- to long-term to minimize the risk to financial stability. The SRB is therefore thought to be a suitable and effective measure to counter the inherent volatility of the Icelandic economy.</p> <p>Less significant credit institutions will be given time to build up own funds to meet the SRB requirements and are not subject to the O-SII buffer. The measure is therefore deemed proportional.</p> <p>The impact of the application of the SRB is thought to be neutral w.r.t. lending growth and own funds requirements of larger, systemically important institutions.</p> |
| 4.5 Justification of inadequacy of existing measures in the CRD or in the CRR, excluding Articles 458 and 459 of the CRR, to address the identified risks (Article 133(11)(e) of the CRD) | <p>The risks addressed by the SRB affect the Icelandic economy and financial system as a whole.</p> <p>Although other measures, such as the other-systematically important institution (O-SII) buffer or the Supervisory Review and Evaluation Process (SREP) Pillar 2 buffer, could be in some conjunction be used to the same effect, none of them offers the economy-compassing horizon of the SRB. The application of the SRB is also deemed the most transparent and clearest measure available to address the risks in question.</p> |
| 5. Cross-border and cross-sector impact of the measure | |
| 5.1 Assessment of cross-border effects and the likely impact on the internal market (Article 133(11)(d) of the CRD and Recommendation ESRB/2015/2) | <p>Since the credit institutions affected by the measure are all largely domestic in terms of operating income and exposures, and relatively small in terms of financial institutions in other countries, any possible cross-border effects stemming from the domestic institutions are likely to be negligible.</p> |

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| 5.2 Assessment of leakages and regulatory arbitrage within the notifying Member State | <p>The credit institutions affected by the measures are all mostly domestic in terms of operating income and exposures. Reciprocation of the measure by EEA countries would limit the potential leakages and regulatory arbitrage further.</p> |
| 5.3 Reciprocation by other Member States (Article 134(4) of the CRD and Recommendation ESRB/2015/2) | <p>The Financial Supervisory Authority of Iceland (FME) intends to formally request reciprocation of the buffer to other states that are members of the European Economic Area (EEA) and which banks provide direct cross-border lending to Iceland to apply an equal or equivalent requirement to those exposures.</p> <p>The systemic risk buffer is intended to increase the resilience of credit institutions in Iceland and counter the increased risk stemming from the inherent structure and small size of the Icelandic economy. These risks affect all domestic credit exposures.</p> <p>In order to avoid leakages and regulatory arbitrage and safeguard competition in credit markets in Iceland reciprocation of the buffer is needed within the EEA.</p> |
| 6. Combination of the SRB with other buffers | |
| 6.1 Combination with G-SII and/or O-SII buffers (Article 133(4) and (5) of the CRD) | <p>There are no Global Systemically Important Institutions in Iceland</p> <p>Three institutions have been identified as systemically important for the Icelandic economy (O-SIIs) having regard to EBA guidelines (EBA/GL/2014/10). An O-SSI buffer of 2% will be applied to those institutions, which will also maintain the SRB.</p> <p>Since the SRB is applied to domestic exposures only it is cumulative with the O-SII buffer for the three systemically important institutions.</p> |
| 6.2 Other relevant information | |
| 7. Miscellaneous | |
| 7.1 Contact person(s) at notifying authority | <p>Mr. Einar Jón Erlingsson Tel: +354 520 3735 einarjon@fme.is</p> |
| 7.2 Any other relevant information | |