

Statement by the Financial Supervision Committee on financial supervision priorities during the COVID-19 pandemic

8 April 2020

The Central Bank of Iceland has adopted a broad range of measures to enable the financial system to provide strong support to Icelandic households and businesses. Interest rates have been lowered, as have minimum reserve requirements; overall requirements for financial institutions' capital base have been eased with the reduction of the countercyclical capital buffer; and sufficient liquidity has been ensured. The Central Bank has repeatedly stated its commitment to being a strong and active supporter of the financial system during the current situation.

In its activities, the Financial Supervision Committee of the Central Bank will do its utmost to support the measures taken by the authorities to assist households and businesses.

General

It is necessary that the Central Bank of Iceland Financial Supervisory Authority (FSA Iceland) continues to receive regular reports from supervised entities, so that it can assess their position, the problems they are addressing, and the risks they are facing. FSA Iceland is prepared, however, to provide some flexibility on deadlines for submittal of such reports and invites supervised entities to contact their FSA Iceland liaison if the need arises. It is appropriate to note that as before, requests will be made for all data that the Central Bank needs in order to evaluate and respond to the current situation. Insofar as is possible, attempts will be made to use the data that supervised entities themselves rely upon in their analyses, as it is assumed that supervised entities have increased the frequency of their in-house analyses and their reporting to management.

Furthermore, in its supervisory activities, FSA Iceland will attempt to give consideration to those supervised entities (or units within such entities) that need to concentrate on addressing imminent operational difficulties caused by the COVID-19 pandemic.

It is well to note that uncertainty can result in an increase in money laundering, fraud, and other economic crimes. The changed conditions resulting from COVID-19 – including closure of bank branches, teleworking by employees, and rapid changes in market prices – could prompt those who engage in such conduct to find new avenues for their criminal activities. Therefore, FSA Iceland wishes to point out to supervised entities that they should remain vigilant vis-à-vis money

laundering and other criminal conduct and should report suspicious transactions to the police.

Sound and proper business practices

FSA Iceland monitors the business practices of supervised entities as they pertain to investors and consumers of financial services, as well as providing information and guidance to them. Now, as before, it is vital to stand guard of sound and proper business practices and to ensure that entities operate honestly and justly and conduct business in a diligent and professional manner, with the interests of their customers and the credibility of the financial market as guiding principles. Because many companies that provide various types of financial services have closed their operational locations, the provision of service has shifted swiftly and almost entirely to mobile devices and other digital solutions. Under such circumstances, it is important to provide thorough and careful assistance and guidance to customers who have difficulty with such solutions or are unaccustomed to using them.

Information on key issues of concern to consumers as regards business practices and consumer protection can be found on a separate COVID-19 information page on the Central Bank website.

Banks and other credit institutions

Banks and other credit institutions play an important role in mediating financing, and in the current circumstances this role is put to the test. The banks are expected to participate actively in the Government measures designed to ensure that they continue to grant loans to their customers and offer restructuring to viable companies. The Financial Supervision Committee emphasises the fundamental principle of prudence and accounting: that short- and long-term risk must be accounted for accurately in credit institutions' balance sheets. FSA Iceland will apply general temporary easing measures, such as allowing institutions to classify frozen mortgages as performing loans if the credit institution concerned deems it likely that the borrower will be able to service the debt satisfactorily after the freeze is lifted. FSA Iceland will publish further guidelines on classification and labelling of loans in due course. Credit institutions will be required, as they have been to date, to assess borrowers' creditworthiness and debt service capacity after this temporary situation eases.

FSA Iceland supports the European Banking Authority's (EBA) 25 March 2020 [Statement on the application of the prudential framework regarding default, forbearance, and IFRS9 in light of COVID-19 measures](#), and it encourages credit institutions to use the Statement as a reference. According to the Statement, it is not automatically necessary to classify loans that have benefited from general measures due to COVID-19 as forborne exposures. The main substance of rules in this area is that such classification should be handled on a case-by-case basis. By the same token, when a loan is classified as performing or non-performing, an assessment needs to be made of whether the borrower is unlikely to be able to pay. As regards banks that prepare annual financial

statements in accordance with international financial reporting standards (IFRS), it is important to assess whether credit risk has increased significantly since the exposure was first recorded (transfer to level 2), either on a per-borrower basis or on a collective basis. It is important that the selection of scenarios in the application of IFRS9 reflect the general expectation that the current situation is temporary, whereas the impact assessment must be conducted on a medium- and long-term basis. The standard provides for a certain flexibility, and it is crucial that credit institutions use it, so that a sudden, significant change in precautionary entries between periods will not result in a contraction in lending, which would amplify the economic downturn.

Systemically important banks are currently conducting their annual supervisory review and evaluation process (SREP). In view of the ongoing difficulties, final decisions on capital requirements will presumably be made based on financial statements later this year rather than as of year-end 2019. Furthermore, no conventional stress test will be conducted at this time in connection with SREP.

In lifting the countercyclical capital buffer, the Central Bank made a move to accommodate financial institutions, for the benefit of households and businesses in Iceland. If financial institutions need nevertheless to tap their capital buffers, the Financial Supervision Committee wishes to point out that by law, if an institution does access its capital buffers, its authorisation to pay out dividends or employee bonuses, or to make other payments or take other measures that would reduce its capital base, is restricted. Furthermore, FSA Iceland can restrict such payments in their entirety, provided that specified statutory requirements are met.

The Financial Supervision Committee also wishes to express its support for EBA's 31 March 2020 [Statement on dividends distribution, share buybacks, and variable remuneration](#). In that Statement, EBA urges financial institutions to observe moderation and refrain from paying dividends or buying their own shares, so as to maintain a strong capital position. Furthermore, EBA encourages financial institutions to review their employment terms policies, partly in consideration of the current economic conditions.

Securities markets and funds

Because of steep price declines and increased volatility in securities markets, FSA Iceland's market supervision has recently placed greater emphasis on supervision of potential market-related fraud (insider fraud and market abuse), margin calls and market conduct, the scope of short sales, issuers' information disclosure requirements, and cessation of trading. Redemptions of mutual funds and investment funds are monitored closely, and daily reports on redemptions by Iceland's largest fund management companies have been requested.

It should be noted that the European Securities and Markets Authority (ESMA) and EFTA Surveillance Authority (ESA) have decided that the threshold for notification of short sales of listed shares should be

reduced from 0.2% of issued share capital to 0.1%. An [announcement](#) to this effect was published on the Central Bank website on 16 March 2020. Attention should also be given to ESMA's 12 March 2020 press release recommending that entities in the securities market take measures to ensure business continuity and comply with risk management requirements due to the COVID-19 pandemic.

Pension funds

The key uncertainty in the pension funds' activities centers on financial market developments and prospects, and the resulting long-term impact on the pension funds' asset portfolios. Sustained declines in asset prices can affect the pension funds' actuarial position, and FSA Iceland is monitoring the situation closely.

Among the provisions of Act no. 25/2020, which amends various other acts of law in response to the economic impact of the COVID-19 pandemic, is an authorisation for individuals to withdraw third-pillar pension savings over a 15-month period. Pension funds and other third-pillar savings custodians must ensure that they have enough liquidity to cover increased withdrawals and assess the impact on the liquidity of their third-pillar savings options. If third-pillar pension savings withdrawals are large enough in scale that it becomes impossible to ensure equal treatment among pension fund members, custodians are authorised to delay the payments, provided that they satisfy certain conditions and obtain prior approval from FSA Iceland.

Issuance of real estate-backed mortgages is an important part of pension funds' investments and the service they provide to fund members. Under current circumstances, pension funds must continue to assess fund members' creditworthiness and debt service capacity, as decisions must be taken on various matters, including deferral of instalments and amendments to terms and conditions. The Financial Supervision Committee considers it appropriate that the pension funds assess whether their lending rules are appropriate in the current climate, and amend them as applicable.

Insurance companies

Insurance companies are faced with a wide range of challenges as a result of COVID-19 and the situation prevailing in the financial markets. Because of both short- and long-term uncertainty, the Financial Supervision Committee emphasises that companies should observe the utmost caution with respect to operational risk and ensure that service to their customers is disrupted as little as possible. Furthermore, FSA Iceland has encouraged insurance companies to adopt appropriate measures to shore up their resilience. In the recent past, there has been considerable strain on communications between providers of travel insurance and their customers, and insurance companies have set up special information pages on their websites in order to share important information on travel insurance and the scope of coverage. The

Financial Supervision Committee reiterates the importance of responsible customer care and efficient handling of insurance claims. FSA Iceland wishes as well to draw attention to the European Insurance and Occupational Pensions Authority's (EIOPA) [2 April 2020 Statement](#) on dividend payments and share buybacks. In the Statement, EIOPA recommends that insurance companies temporarily postpone all dividend payments and share buybacks because of the uncertainty caused by COVID-19.