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MREL - POLICY

CENTRAL BANK OF ICELAND RESOLUTION AUTHORITY

SEÐLABANKI ÍSLANDS

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Central Bank of Iceland Resolutioon Authority

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Summary

The Central Bank of Iceland Resolution Authority takes decisions on minimum requirements for own funds and eligible liabilities (MREL) for[1] each credit institution in Iceland[2], based on a resolvability assessment and the resolution plan for the institution concerned.

The MREL requirement comprises the loss absorption amount (LAA) and the recapitalisation amount (RCA).

The loss absorption amount is equal to minimum required own funds; i.e., the sum of Pillar I and Pillar II-R. The recapitalisation amount must be at least equal to minimum required own funds. It is typically supplemented by a so-called market confidence charge (MCC), which is equal to the combined capital buffer requirement with a haircut based on an assessment carried out by EEA resolution authorities. The recapitalisation amount is 0 for financial institutions that undergo conventional winding-up proceedings.

Highlights of the Central Bank of Iceland Resolution Authority's MREL requirements

- The loss absorption amount (LAA) is equivalent to minimum required own funds (Pillar I and Pillar II-R).
- Financial institutions are notified of their MREL requirements excluding the combined capital buffer requirement and must satisfy the latter alongside the MREL.
- The recapitalisation amount (RCA) is equivalent to minimum required own funds.
- It is permissible to satisfy the recapitalisation amount using common equity Tier 1 capital or other capital instruments in excess of total required own funds.
- When an assessment is made of whether a financial institution satisfies weighted MREL requirements, it is prohibited to include common Tier 1 capital that is maintained in order to satisfy capital buffer requirements.
- At the present time, no market confidence charge (MCC) will be levied in Iceland.
- If the preferred resolution strategy according to an institution's resolution plan entails measures other than bail-in, it is permissible to adjust MREL requirements downwards relative to those of firms for which bail-in is the preferred strategy.
- Financial institutions in Iceland must satisfy requirements concerning eligible liabilities and subordination at any given time.
- The Resolution Authority urges financial institutions to acquaint themselves with the provisions concerning the grant of a longer MREL transition period and restrictions on distributions if an institution does not satisfy its MREL.
- A more detailed summary can be found on pages XX-YY.

1. MREL stands for Minimum Requirement for Own Funds and Eligible Liabilities, often referred to as MREL or MREL requirement(s).
2. In the discussion of MREL in this policy, the term "financial institution" is used as a blanket term for entities subject to MREL, even though MREL could apply to credit institutions, larger investment firms, and certain holding companies or other sub-consolidated entities of these institutions.

1

Legal framework[3]

Chapter IV of the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, discusses minimum requirements for own funds and eligible liabilities (MREL or MREL requirements).[4] MREL requirements entail that, in addition to total required own funds (i.e., in addition to the Central Bank's capital buffers and the minimum required own funds),[5] the composition of a financial institution's funding must be sufficient both for loss absorption and for recapitalisation should the institution be failing or likely to fail. The Central Bank of Iceland Resolution Authority determines MREL requirements in accordance with Article 17 of Act no. 70/2020, with reference to the activities and position of each individual financial institution, and with an eye to achieving the objectives of resolution according to Article 1 of the Act. Furthermore, the methodology for calculating MREL has been harmonised within the EEA with the second Bank Recovery and Resolution Directive (BRRD II), which has been implemented in Iceland.

1.1. The Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020

Chapter IV of Act no. 70/2020 covers MREL requirements. MREL requirements entail a defined and separate minimum ratio of funds (i.e., own funds and liabilities) that banks must maintain at all times. By law, MREL are expressed as the amount of eligible liabilities and own funds as a percentage of total liabilities and own funds, or the total risk exposure amount (TREA, or risk-weighted MREL), cf. Article 92(3) of the Capital Requirements Regulation (CRR), and the total exposure measure (TEM, or non-risk-weighted MREL), cf. Articles 429 and 429a of the CRR.[6] The Resolution Authority determines the percentage in accordance with Article 17, Paragraphs 1-4 of Act no. 70/2020 and the Regulation on the Minimum Requirement for Own Funds and Eligible Liabilities, no. 700/2024.

In order for liabilities to be considered eligible for MREL, they must meet certain criteria. They must be considered suitable for bail-in; i.e., financial instruments or obligations that are not part of own funds and are not excluded from bail-in according to Article 56 of Act no. 70/2020. In addition, they must satisfy the requirements laid down in Article 17, Paragraph 2 of Act no. 70/2020; cf. also Articles 72a-72c of the CRR. Among other requirements, the liabilities must be paid in, and they may neither be liabilities vis-à-vis the financial institution itself nor be guaranteed by or otherwise the responsibility of the financial institution itself. Furthermore, they may not have been funded directly or indirectly by the institution itself, and the residual maturity must be at least one year. Further discussion of eligible liabilities can be found in Section 4 of this Policy.

3. All legal authorisations in effect at any given time concerning MREL, the application of resolution measures, and the activities of the Central Bank of Iceland Resolution Authority can be found on the Resolution Authority website.

4. For simplification, this policy generally uses the acronym MREL (or MREL requirement) instead of the legal term *minimum requirement for own funds and eligible liabilities*. This applies not least to discussions of the minimum requirement as a ratio, or MREL requirement(s), as regards total requirements relating to MREL; i.e., the ratio together with, for instance, requirements for eligible liabilities.

5. In this MREL Policy, the discussion and use of terminology on financial institutions' capital requirements is aligned with that in the *Common procedures and methodologies for the supervisory review and evaluation process (SREP Guidelines)*. Further information can be found here, particularly to include page XX.

6. Regulation (EU) no. 575/2013 on prudential requirements for credit institutions and investment firms (the Capital Requirements Regulation, CRR) has been incorporated into Icelandic law on the basis of Article 1(c) of the Act on Financial Undertakings, no. 161/2002. It is generally referred to as the CRR in this MREL Policy.

The Resolution Authority makes the final decision on MREL for each financial institution; cf. Article 17, Paragraph 3 of Act no. 70/2020. The decision must be based on the following points, at a minimum:

1. The institution's resolution action can be completed by applying appropriate measures, including bail-in if applicable, in a manner that achieves the objectives of resolution according to Article 1 of Act no. 70/2020.
2. The institution's eligible liabilities are sufficient to ensure that, upon application of the bail-in tool, its loss absorbency will be adequate and the CET1 capital ratio can be restored so that the institution satisfies the requirements for an operating licence and retains market confidence.
3. The institution's eligible liabilities, other than those that could fall outside the scope of the bail-in tool according to Article 56, Paragraph 2 of Act no. 70/2020, or those that could be transferred as a whole according to the institution's resolution plan, are sufficient to ensure that its loss absorbency will be adequate and the CET1 capital ratio can be restored so that the institution satisfies the requirements for an operating licence.
4. The institution's size, business model, funding model, and risk profile.
5. The impact of the insolvent institution on financial stability, including the impact due to its interconnectedness with other credit institutions or investment firms, or with other parts of the financial market.

The decision on MREL shall take into account that the requirement is intended to support resolution actions, if the conditions for such actions are satisfied. The decision shall also take into account that if resolution action is taken, the financial institution must have sufficient eligible liabilities to ensure that its loss absorbency will be adequate and its own funds can be restored so that the institution satisfies the requirements for an operating licence.

Furthermore, the decision on MREL shall take into account the institution's size, business model, funding model (i.e., how it handles its funding), and risk profile. Finally, the decision shall take into consideration the impact on financial stability should the institution become insolvent. To this end, consideration shall be given to interconnectedness with other financial institutions or even with other parts of the financial system, and to potential contagion among institutions.

During the run-up to such a decision, the Central Bank Resolution Authority must consult with the Central Bank's financial supervisory authorities; cf. Article 4, Paragraph 3 of Act no. 70/2020.

1.2. The MREL Regulation

Harmonised criteria for the calculation of MREL are presented in the Regulation on the Minimum Requirement for Own Funds and Eligible Liabilities, no. 700/2024 (the MREL Regulation). With the adoption of the Regulation and the passage of Act no. 63/2023 Amending the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, BRRD II[7] was incorporated in full into Icelandic law. According to the MREL Regulation, the Resolution Authority has some scope, albeit limited, to conduct its own assessment and take decisions on individual elements of MREL.

The MREL Regulation determines the elements of own funds requirements that must be considered when MREL are set; i.e., the loss absorption amount (Article 10, Paragraph 1(a), Point (i) of the Regulation) and the recapitalisation amount (Article 10, Paragraph 1(a), Point (ii)). The Regulation also specifies (in Article 9) that the Resolution Authority shall assess and determine MREL based on the following:

- Whether any specific liabilities will be explicitly excluded from bail-in on the basis of the authorisation in Article 56, Paragraph 2;
- The institution's risk profile, business model, and funding structure; and
- The institution's size and systemic risk.

7. Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms.

It can be construed from Article 10, Paragraph 1(a) of the MREL Regulation that the point of departure for the methodology is that the minimum MREL ratio must be equal to double the overall requirement for own funds. The ratio is intended to ensure that if an institution is failing or likely to fail, it can continue to operate following resolution and will satisfy the same requirements as were made of it before it failed. On the other hand, the Regulation offers options for adjusting amounts, provided that certain conditions are satisfied. This applies to both the loss absorption amount and the recapitalisation amount.

On the basis of Article 10, Paragraphs 6-8 of the MREL Regulation, it is possible to adjust the loss absorption amount, so that it could exceed the total own funds requirement. In such instances, an additional amount, the market confidence charge (MCC), is added so as to maintain market trust after resolution. The MCC shall generally be equal to the combined own funds requirement that is to apply after the application of resolution measures, less the countercyclical capital buffer value. However, on the basis of Article 10, Paragraph 9 of the MREL Regulation, it is possible to lower the MCC if a smaller amount can maintain market confidence, as well as guaranteeing the continuation of critical functions and access to funding without extraordinary financial support other than a contribution from the resolution fund. In addition, the recapitalisation amount may be lower or higher on the grounds that all or some currently applicable Pillar II-R requirements will no longer apply after the preferred resolution action has been implemented. It is also permissible under Article 10, Paragraph 5 of the Regulation to adjust the value of risk-weighted assets. Among European countries, the adjustment commonly equals about 10% of risk-weighted assets.

It is intended that the Resolution Authority will ensure that MREL are sufficient, given that certain liabilities could be excluded from bail-in; cf. Article 56, Paragraph 2 and Article 57, Paragraph 1 of Act no. 70/2020, or that they may be partially disposed of via other resolution measures (asset sales or a bridge institution); cf. Articles 9 and 13 of the MREL Regulation. The assessment of whether MREL are sufficient is carried out, on the one hand, by determining whether the liabilities in question satisfy the requirements of Article 56, Paragraph 2 of Act no. 70/2020 and therefore cannot support the institution's loss absorption and recapitalisation, and on the other hand, by determining whether excluding or transferring liabilities, irrespective of whether they can be included in MREL, could be in breach of the "no creditor worse off" (NCWO) rule. Under the NCWO rule, resolution of a financial institution may not put any creditor in a weaker position than it would have been in had the institution undergone conventional winding-up proceedings. In addition, upon determining MREL, cf. Article 9 of the MREL Regulation, the Central Bank Resolution Authority will take into account Articles 56-57 of Act no. 70/2020 as a whole, including provisions on contributions from a resolution fund because of liabilities that are excluded from bail-in.

1.3. Sanctions and coercive measures in connection with MREL (MREL maximum distributable amount, M-MDA)

With the passage of Act no. 63/2023, financial institutions were subjected to the requirement that they limit specified distributions that affect own funds if the institution does not satisfy MREL in addition to capital buffers (referred to as MREL maximum distributable amount rules, or M-MDA[8] rules). These distributions include dividend payments, share buybacks, bonus payments, and retirement of AT1 instruments. The provisions applying to calculation of M-MDA are laid down in Articles 20 and 21 of the MREL Regulation. They are similar to the rules applying to calculation of the maximum distributable amount and restrictions on distributions relating to capital buffers; cf. Articles 5-6 of the Rules on the Maximum Distributable Amount and Restrictions on Financial Undertakings' Distributions in Connection with Capital Buffers, no. 1270/2015. Therefore, when a determination is made of how much a financial institution's distributions should be restricted, it is important to consider the extent to which the institution falls below the combined buffer requirement when the requirement is assessed with reference to the institution's MREL position.

Capital buffers are not part of the loss absorption amount in MREL. The capital buffer requirement is independent and exists alongside MREL requirements. However, MREL are always assessed with an eye to whether

8. M-MDA stands for MREL maximum distributable amount.

and how the financial institution satisfies the combined capital buffer requirement. A situation could arise wherein a financial institution does not satisfy its MREL in full but does satisfy the Central Bank's total own funds requirement. Under such circumstances, the institution generally has sufficient capital instruments but does not have enough additional capital instruments or eligible liabilities to satisfy the MREL. By the same token, it is possible that an institution will satisfy its MREL when that requirement is examined in isolation, but not when it is examined together with the combined capital buffer requirement. In this case, the institution generally has enough eligible liabilities but has insufficient capital instruments.[9]

As is stated in Article 20 of the MREL Regulation, a number of criteria apply as regards the factors that must be considered in setting restrictions on distributions when a financial institution does not satisfy its MREL in addition to its capital buffer requirements. These criteria apply in particular to the determination of measures upon receipt of notification from a financial institution in accordance with Article 20, Paragraph 1 of the Regulation. The Resolution Authority will take account of criteria according to Article 20, Paragraphs 4 and 6 – i.e., as regards the institution's position and the outlook for the markets – when assessing whether and how to apply M-MDA restrictions.

In addition to the restrictions due to MREL, the Central Bank is authorised to levy administrative fines on financial institutions in connection with MREL. If a financial institution does not satisfy the minimum requirement for own funds and eligible liabilities or does not take steps to restrict distributions related to MREL, the Bank may impose an administrative fine on the institution in question; cf. Article 94 of Act no. 70/2020.

Furthermore, the Resolution Authority may demand that a financial institution issue eligible liabilities or take other action, such as renegotiating the terms and conditions of eligible liabilities so as to satisfy MREL requirements; cf. Article 15, Paragraph 3, Items 10 and 11 of Act no. 70/2020.

9. For further information, see Chapter 8 of the European Single Resolution Board's MREL Policy, which can be found here.

2

MREL: role and methodology

The aim of MREL is to ensure that financial institutions have sufficient capital to guarantee both loss absorption and recapitalisation should the need arise.[10] MREL are therefore intended to ensure that instead of bailing a failed financial institution out using Government funds, it will be possible to bail in and recapitalise it using creditors' funds. A further objective of MREL is to ensure that a financial institution's liabilities are not excluded from bail-in.

The Central Bank Resolution Authority may require that a financial institution's funding – i.e., its own funds and liabilities – equal a specified amount and satisfy specified criteria so as to ensure that the institution can be recapitalised if it fails. MREL requirements thereby have a dual function: They ensure that financial institutions have adequate loss absorption capacity and that they can be recapitalised. Capital shall be sufficient to cover the institution's losses and ensure that, after appropriate resolution action is taken, it has enough own funds to retain its operating licence and carry out critical functions.

2.1. Relationship between MREL and financial institutions' resolvability assessments and resolution plans

The Resolution Authority determines MREL requirements on an institution-specific basis, and the decision shall ensure that the requirements support the institution's resolution action in accordance with the resolution plan. Although MREL methodology is harmonised within Europe on the basis of the MREL Regulation, decisions are always taken on an institution-specific basis, taking account of the activities and asset portfolio of the institution concerned. Based on the resolution plan for the institution, including the selected resolution strategy, the Resolution Authority takes a decision on that institution's MREL.

MREL are determined with an eye to the preferred resolution action for each institution. The preferred resolution action is selected following an analysis of the institution's operations, which is carried out at the time of its resolvability assessment. When this process is complete, a decision is taken on MREL, concurrent with the approval of the resolution plan. In particular, the preferred resolution strategy is determined based on which of the institution's critical functions should be protected, as well as an assessment of those functions' substitutability; i.e., whether the functions can be carried out by another financial institution or financial market entity.

Those financial institutions that do not satisfy the conditions for resolution – for instance, the requirement that resolution be considered necessary in the public interest – are placed in conventional winding-up proceedings pursuant to the Act on Financial Undertakings and will only be required to satisfy general capital requirements; i.e., the total requirement for own funds. If the institution can be subjected to winding-up proceedings immediately on the basis of the resolvability assessment, this means that the MREL requirements will not exceed that institution's own funds requirements.

The institution's resolution plan specifies the preferred resolution strategy for its operations; i.e., the resolution action considered preferable should the institution be failing or likely to fail. Apart from bail-in, it is possible to apply other resolution measures, such as selling part or all of the assets of an institution that is failing or likely to fail, or creating a bridge institution that takes over the failing institution's activities.. If a resolution action other

10. MREL apply to European banks and are based on the Total Loss Absorption Capacity Standard (TLAC Standard), issued by the Financial Stability Board (FSB). Further information on TLAC and minimum loss absorption requirements for global systemically important banks can be found on the FSB website.

than bail-in is considered the most preferable according to the resolution plan, it is permissible to adjust the institution's MREL downwards; cf. Chapter 3.5.

2.2. General information on MREL methodology

According to Article 2 of the MREL Regulation, MREL are presented in two ways – risk-weighted and non-risk-weighted. In both cases, the numerator in the formula used for MREL calculation is the sum of own funds and eligible liabilities. The requirement is calculated either as a percentage of this amount divided by the institution's risk-weighted assets (risk-weighted MREL) or as total assets (non-risk-weighted MREL). Most often, discussions of MREL refer to risk-weighted MREL.[11] For Icelandic credit institutions, risk-weighted MREL are more onerous and therefore set boundaries for the institutions as regards sufficient own funds and eligible liabilities.

The rule of thumb for calculating MREL is that the MREL shall equal at least double the minimum own funds requirement (two times Pillar I and Pillar II). Combined buffer requirements (CBR) are excluded from the calculation of the MREL ratio and constitute a separate requirement. Credit institutions must therefore satisfy MREL and capital buffer requirements simultaneously.

Non-risk-weighted MREL are calculated as the sum of own funds and eligible liabilities, expressed as a percentage of total exposures.[12] They shall be at least 6%, which is equivalent to double the minimum required leverage ratio (3%). In calculating non-risk-weighted MREL, it is permissible to include own funds held for the combined capital buffer requirement (CBR).

Through the years, however, individual countries within the EEA have used different formulae to determine MREL.[13] Virtually all European countries have imposed a market confidence charge (MCC) on financial institutions. Within the EEA, the MCC is equal to the sum of capital buffers less the countercyclical capital buffer value. In the UK, however, no MCC is levied.

As a result, it can generally be said that MREL requirements depend on the minimum own funds requirement, on the one hand, and how high the capital buffers are, on the other. The total own funds requirement is therefore the main determinant of the final MREL requirement.

2.3. Loss absorption amount

The MREL Regulation assumes that the benchmark for calculating the loss absorption amount (LAA) shall be presented as the sum of these items:

1. the Pillar 1 own funds requirement according to Article 92(1) of the CRR; and
2. the additional Pillar II own funds requirement provided for in Article 86(g), Paragraph 4 of the Act on Financial Undertakings.

As has previously been noted, financial institutions must always satisfy the combined capital buffer requirement, which is separate from MREL requirements.

2.4. Recapitalisation amount and market confidence charge

It can be inferred from Article 9 of the MREL Regulation that the recapitalisation amount (RCA) must be able to support the preferred resolution action according to each financial institution's resolution plan. This amount is based on which resolution measures are assumed to be applied in connection with the preferred resolution action. The recapitalisation amount could be zero (0) if the resolvability assessment for an institution suggests that it is both realistic and economical to place the institution in conventional winding-up proceedings; i.e., if it is not

11. In this Policy, the term MREL generally refers to risk-weighted MREL unless explicitly stated otherwise.
12. The total exposure measure (TEM) is used in particular for the calculation of banks' leverage ratios.
13. In this context, it is worth noting that under BRRD I, Denmark, Norway, and Sweden all developed their own versions of the MREL formula. Their point of departure was that MREL should be approximately double the total own funds requirement (i.e., Pillar I x 2, Pillar II x 2, and capital buffers x 2).

assumed that the institution will undergo resolution. For such institutions, MREL will be equal to the loss absorption amount. For financial institutions that undergo resolution, the recapitalisation amount will consist of two factors:

1. The amount that is required, after the implementation of the preferred resolution action, to enable the institution to satisfy the minimum own funds requirement and the appropriate leverage ratio requirement, but without any capital buffer requirement; and
2. an additional amount that the resolution authority considers adequate to maintain market confidence following resolution. This amount shall generally be equal to the combined capital buffer requirement excluding the countercyclical capital buffer value. However, the market confidence charge may be lower than the combined requirement (although not lower than zero) if the resolution authority considers the amount sufficient to maintain market confidence, support critical functions, and ensure adequate funding for the institution.

The MCC is the MREL component that has perhaps varied the most from one European country to another in recent years. It is a subjective factor that resolution authorities have been able to determine based on specified ground rules. For instance, in the BRRD I environment, Denmark applied a market confidence charge equal to the combined capital buffer requirement with no haircut, whereas the Single Resolution Board, Norway, and Sweden applied various types of haircut. The Single Resolution Board's methodology based on BRRD I assumed that the market confidence charge would be the combined capital buffer requirement, less 1.25% of risk-weighted assets. [14]In Norway, the corresponding haircut was the countercyclical capital buffer value at any given time.[15] In Sweden, capital buffers were not included in the market confidence charge portion of the recapitalisation amount, but offsetting this, Swedish banks were prohibited from using retained earnings to satisfy MREL requirements.[16] In the UK, it was decided not to impose a market confidence charge.[17]

With BRRD II, the calculation of the MCC was harmonised within the EEA, and with the passage of Act no. 50/2022 and the MREL Regulation, which implemented BRRD II in Iceland, the calculation of the MCC was adapted to that practice. The general rule is that the market confidence charge is equal to the combined capital buffer requirement, less the countercyclical capital buffer value at any given time. Nevertheless, resolution authorities within the EEA are still authorised to adjust that amount upwards or downwards, provided that it is ensured that the MCC: i) maintains market confidence; ii) can sustain critical functions; and iii) can guarantee short-term funding; i.e., until access to market funding is re-established (12 months).

2.5. Impact on MREL stemming from resolution actions other than bail-in

The purpose and objective of MREL is to ensure that appropriate resolution action can be taken vis-à-vis a financial institution undergoing resolution. The determination of which resolution actions are appropriate is based on each financial institution's resolvability assessment and resolution plan; in other words, the selection of the preferred resolution strategy. In general, MREL methodology is based on ensuring that the bail-in tool can be applied during resolution. If the preferred resolution strategy entails the application of other tools – i.e., asset sales, a bridge institution, or asset separation – the MREL are adjusted. In such instances, the Resolution Authority adjusts financial institutions' risk-weighted assets by 10-25% when determining their MREL. The determination of how large an adjustment is bade is based on the Resolution Authority's assessment of how the financial institution satisfies the criteria for the application of resolution measures other than bail-in; e.g., as regards management information systems (MIS), access to data, analysis of potential buyers, and separability analysis.

14. Further information on the Single Resolution Board's methodology under BRRD I can be found here. Information on the Single Resolution Board's methodology under BRRD II can be found here.
15. Further information on the methodology used by Finanstilsynet in Norway can be found here.
16. The methodology used by Riksgälden in Sweden changed in 2021, but the method under BRRD I entailed not applying a market confidence charge; i.e., not including it in the recapitalisation amount. Further information on the methodology used by Riksgälden in Sweden under BRRD II can be found here.
17. Further information on the methodology used by the Bank of England to determine MREL can be found here.

3

Eligible liabilities and subordination

MREL entail requirements regarding the amount of own funds and eligible liabilities. This involves ensuring that own funds and liabilities can be used for loss absorption and recapitalisation in accordance with the preferred resolution strategy selected by the resolution authority. Because of this, MREL requirements lay down conditions that financial institutions must satisfy as regards liabilities, so that they will be deemed eligible. This section of the Central Bank Resolution Authority's MREL Policy focuses on the requirements made of eligible liabilities. It also discusses the Resolution Authority's position on issues relating to eligible liabilities, particularly as regards subordination and the possibility of using unsecured (i.e. senior preferred) debt instruments to satisfy MREL requirements.

3.1. Definitions of eligible and bail-inable liabilities

The terms *bail-inable liabilities* and *eligible liabilities* are linked, and both are defined in Article 3, Paragraph 1 of the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020. In order for liabilities to be considered *bail-inable*, they must satisfy two main conditions:

1. They must be financial instruments or liabilities that do not comprise the capital base (own funds) as provided for in the Act on Financial Undertakings; and
2. they must be excluded from bail-in on the basis of Article 56, Paragraph 1 of Act no. 70/2020.

Liabilities that are excluded from bail-in are listed in Article 56, Paragraph 1 of Act no. 70/2020. It is prohibited to apply bail-in to the following liabilities:[18]

1. Guaranteed deposits pursuant to the Act on Deposit Guarantees and an Investor-Compensation Scheme.
2. Guaranteed liabilities, including covered bonds pursuant to the Act on Covered Bonds, and financial instruments that are intended for hedging and included in a collateral portfolio and that enjoy the same legal protections as covered bonds.
3. Liabilities arising from assets that an institution or unit administers on behalf of its customers, including the assets of investment funds and alternative investment funds – cf. the Act on Investment Funds and the Act on Alternative Investment Fund Management Companies – and are protected pursuant to Article 109 of the Act on Bankruptcy, Etc.
4. Liabilities arising from a custodial relationship between an institution or unit and a rights holder, provided that the rights holder is protected pursuant to Article 109 of the Act on Bankruptcy, Etc., or other legislation.
5. Liabilities owed to companies other than those in the same group and due within seven days.
6. Liabilities owed to payment and settlement systems and due within seven days, cf. the Act on the Security of Transfer Orders in Payment Systems and Securities Settlement Systems, or owed to participants in such systems and deriving from their participation in those systems.

18. In addition to the specified liabilities, the Central Bank may, on the basis of Article 56, Paragraph 2 of Act no. 70/2020, exclude liabilities other than those listed in that provision; for instance, if it is not possible to apply the bail-in tool to liability within a reasonable length of time. In taking such a decision, the Resolution Authority consults the criteria laid down in Commission Delegated Regulation (EU) 2016/860; cf. the Regulation on the Entry into Effect of EU Regulations on Resolution Procedures for Credit Institutions and Investment Firms, no. 95/2021.

7. Obligations to employees, including accrued unpaid wages, pension fund contributions, accrued vacation pay and other employment-related items, but excluding bonuses unless they are provided for in general wage agreements.
8. Accounts payable due to the purchase of goods and services that are necessary for the institution or unit's day-to-day operations.
9. Liabilities vis-à-vis the tax authorities and the social security scheme if they enjoy priority in the insolvency hierarchy.
10. Unpaid contributions to the Financial Institutions' Insurance Fund (TVF); cf. the Act on Deposit Guarantees and an Investor-Compensation Scheme.

Bail-inable liabilities are considered eligible for MREL if they satisfy the requirements laid down in Article 17, Paragraph 2 of Act no. 70/2020. Eligible liabilities also include subordinated loans that satisfy the requirements for classification as Tier 2 capital pursuant to the Act on Financial Undertakings but are not used for Tier 2, provided that they have a residual maturity of more than one year.

According to Article 17, Paragraph 2 of Act no. 70/2020, eligible liabilities must satisfy all requirements laid down in Articles 72a, 72b, and 72c of the CRR, *except that they need not satisfy the subordination requirement according to Article 72b(2), Point (d)*.

The following are among the key requirements in question; cf. Articles 72a, 72b, and 72c of the CRR:

1. The financial instrument must be issued and fully paid in.
2. The liability shall not be vis-à-vis the financial institution, nor shall it have been guaranteed by the institution.
3. The purchase of the financial instrument may not have been financed directly or indirectly by the institution.
4. The residual maturity of the liability must be at least one year. The residual maturity of a liability that provides for the right to demand reimbursement before the end of the contract period shall be based on the date such a right first becomes exercisable.
5. The liability may not arise from a derivative.
6. The liability may not arise from a deposit balance that enjoys priority in the claim hierarchy pursuant to Article 85(a), Paragraph 1, Item 1(a) or 1(b) of Act no. 70/2020.

In addition to the above-mentioned requirements, financial institutions must ensure that their liabilities satisfy all fourteen of the requirements listed as Points (a)-(n) in Article 72a of the CRR in order to be considered eligible. Furthermore, various liabilities that are exempt from classification as eligible liabilities, twelve types in all, are listed Points (a)-(l) in Article 72a of the CRR II..

3.2. Subordination

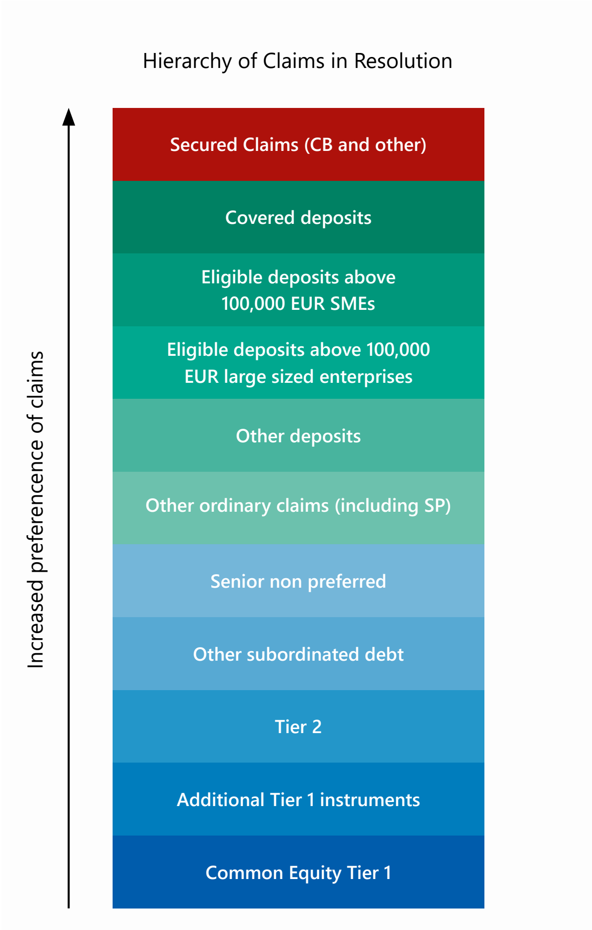
With the implementation of BRRD II in Iceland, with the passage of Act no. 63/2023 Amending the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, and the adoption of the MREL Regulation, a portion of eligible liabilities must be subordinated; i.e., they must rank lower in terms of claim priority than obligations exempt from bail-in. The requirements for subordination are complex and detailed, as they differ according to financial institution type and size. In deciding on subordination, the Resolution Authority considers two types of criteria that could apply.

On the one hand, Article 11 of the MREL Regulation requires that subordination of own funds and subordinated eligible liabilities constitute at least 13.5% of risk-weighted assets. This requirement must be satisfied alongside the combined capital buffer requirement. The provision in question applies to entities that the Resolution Authority has assessed as being relatively likely to cause systemic risk if they should become insolvent. In taking a decision for any given bank, the Resolution Authority considers its share of deposit-based funding, its level of access to funding markets, and the extent to which it relies on CET1 instruments. In addition, the

Resolution Authority considers the general criteria for decisions on subordination as laid down in Article 8 of the Regulation on the Minimum Requirement for Own Funds and Eligible Liabilities, no. 700/2024.

On the other hand, the Authority bears in mind the possibility of adapting subordination requirements to the relevant institution's financial position and MREL on the basis of Article 6 of the MREL Regulation. In assessing the possibility of such an adaptation, the Authority gives particular consideration to the size of the institution in question, whether there is the risk that the no creditor worse off (NCWO) rule will be violated, and the general criteria underlying decisions on subordination as laid down in Article 8 of Regulation no. 700/2024.

With the passage of Act no. 38/2021 Amending the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, the claim hierarchy for resolution and winding-up of financial institutions and Iceland was clearly stipulated. When that Act was passed, it became clear that deposits take priority over senior preferred debt instruments upon the failure of a financial institution. The passage of Act no. 38/2021 incorporated Directive (EU) 2017/2399 into Icelandic law. The law and the directive set requirements for the issuance of senior non-preferred debt instruments provide for their ranking in the claim hierarchy during resolution and winding-up.



Senior non-preferred debt instruments must satisfy all of the following conditions:

- The original contractual maturity must be at least one year.
- The instruments in question must not be derivatives or contain embedded derivatives.
- Their ranking in the claim hierarchy must be provided for in the contractual terms and provisions and in the prospectus for the issue, if applicable.

In light of the claim hierarchy pursuant to the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, senior preferred debt instruments can be included with MREL requirements determined on the basis of Articles 9, 10, and 14 of the MREL Regulation, but they generally are not included with the portions of MREL that entail subordination. The ranking of deposits in the claim hierarchy provided for in Icelandic law makes it realistic to include senior preferred debt instruments with MREL requirements in Iceland. In general, the amount of those liabilities that are equal in rank to senior preferred debt instruments in the claim hierarchy is not high among Icelandic financial institutions. Further information can be found in Section 5.4 of this document.

4

The Central Bank of Iceland's MREL requirements

As can be inferred from Sections 2-4, resolution authorities within the EEA are granted some flexibility in determining MREL requirements. To summarise, this flexibility lies mainly in the following:

- Decisions on the application of resolution measures, particularly the determination of whether bail-in is the preferred resolution action.
- An assessment of each institution's risk profile, funding model, and business model.
- The loss absorption amount and recapitalisation amount (including the market confidence charge) and their interaction with capital buffer values and additional capital requirements made by the Central Bank (Pillar II).
- Subordination and the determination of which liabilities can be included with MREL.
- Deadlines for satisfaction of MREL requirements.

In this section of the MREL Policy, the aim is to present the Central Bank's position on these points, so that the requirements to be made in the determination of MREL will be clear to financial institutions. The point of departure for MREL determination is, and will be, that the ratio must be high enough to ensure that it will be possible to apply the preferred resolution action as presented in each institution's resolution plan.

4.1. Application of resolution measures and classification of institutions with respect to MREL

The Central Bank Resolution Authority is of the view that, in general, bail-in is the resolution action most likely to be applied upon resolution of financial institutions in Iceland. Applying the bail-in tool serves the general purposes of resolution as laid down in the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, more effectively than other resolution measures do; i.e., measures entailing the full or partial disposition of an institution's assets or operations, with or without the establishment of a bridge bank or asset management company during resolution. Bail-in can ensure the swift and efficient recapitalisation of an institution that is failing or likely to fail. As a result, it is most realistic and most likely, if an institution in Iceland should be failing or likely to fail, that bail-in will be used to restore the institution's financial position. The Resolution Authority points out, however, that financial institutions' resolution plans generally include not only the preferred resolution action but also various versions of resolution strategies, including the application of other resolution measures under differing scenarios. Furthermore, financial institutions' size and the nature of their operations will probably affect the preferred resolution strategy. That being the case, it is impossible to state with certainty that only one resolution measure will be selected for all financial institutions in Iceland.

The Central Bank Resolution Authority's methodology in applying the bail-in tool entails placing financial institutions into three broad categories:

- **Category 1** – This category includes institutions whose business model, operations, risk profile, and funding model assume that an open bank bail-in will be the preferred resolution action. The MREL requirements for these institutions are generally determined on the assumption that bail-in will be the only resolution action taken.

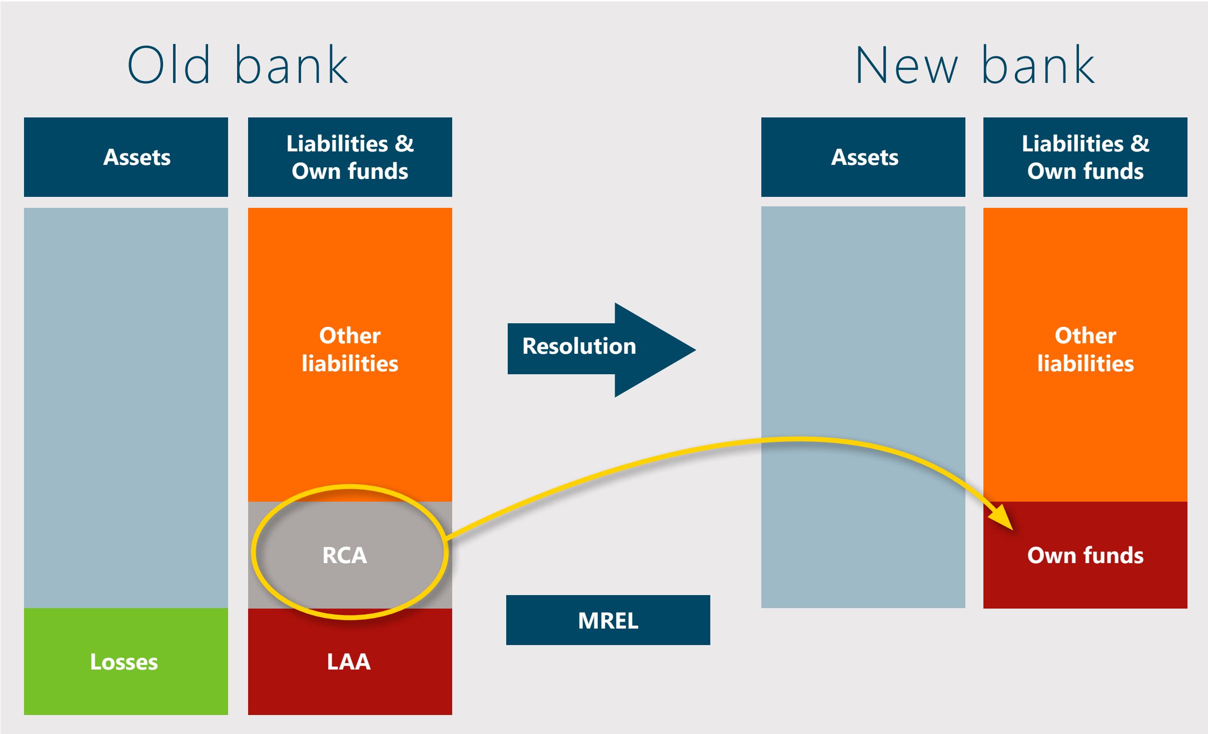


Chart 1. MREL requirements are intended, among other things, to ensure that financial institutions always have sufficient funds to recapitalise their operations if they are failing or likely to fail. The chart illustrates the relationship between MREL requirements and the application of the bail-in tool.

- **Category 2** – This category includes institutions for which a mixed approach to resolution is possible. This implies that it could be considered realistic and economical, in terms of the objectives in the Act on Resolution of Credit Institutions and Investment Firms, to sell operations or dispose of part or all of the institution's assets. In this case, it could be possible to apply a closed bank bail-in tool simultaneously. One of the main conditions for this classification is that only a portion of the bank's operations – i.e., the part where critical functions take place – will be recapitalised, while other operations will be sold or discontinued. Another condition is that conventional winding-up proceedings must be deemed less likely to achieve the objectives laid down in the Act on Resolution of Credit Institutions and Investment Firms; i.e., of preserving financial stability and avoiding a severe negative impact on the financial system. In general, MREL requirements for these institutions will be lower than for Category 1 institutions; cf. Section 3.5.
- **Category 3** – This category includes institutions that do not satisfy the conditions for resolution – i.e., because resolution does not ensure that the objectives of the Act on Resolution of Credit Institutions and Investment Firms will be achieved more effectively than with conventional winding-up proceedings, or because resolution is not considered necessary in the public interest. For these institutions, the recapitalisation amount will be zero and there will be no MREL requirements over and above the ordinary own funds requirements for such institutions.

The aforementioned methodology takes into account the execution and policy formulation practised in neighbouring countries, particularly the Nordic countries and the UK. It can be assumed that institutions that satisfy the requirements for submittal of simple recovery plans, and for which simple resolution plans are prepared, will be placed in Category 3. As regards other institutions, the business plan, operations, risk profile, and funding model will determine in each instance whether the institution is placed in Category 1 or Category 2, provided that critical functions take place in the institution and/or that it could be necessary to take resolution action, cf. Article 35, Paragraph 1 of Act no. 70/2020.

The Central Bank Resolution Authority's MREL Policy and the MREL requirements that will be made of financial institutions in Iceland entail, all else being equal, that resolution will involve a single point of entry (SPE) approach rather than a multiple point of entry (MPE) approach. This implies that the decision to apply resolution measures at the group level will be taken only by the Resolution Authority in Iceland, without the involvement of resolution authorities elsewhere in the EEA. All else being equal, the operations and structure of Icelandic financial institutions are such that the Central Bank Resolution Authority alone will prepare a resolution plan and take decisions on the application of resolution measures for Icelandic financial institutions; no resolution colleges will be involved. If the structure and operating environment should change in this respect, the Central Bank's MREL Policy will be reviewed so as to address new issues that could arise.

4.2. Position on the loss absorption amount and recapitalisation amount

4.2.1. Loss absorption amount

The loss absorption amount corresponds to the overall requirement for own funds. The Central Bank Resolution Authority is prohibited from raising or lowering the default loss absorption amount; cf. Article 10, Paragraphs 5-8 of the MREL Regulation.

The Resolution Authority reiterates, however, that combined capital buffer requirements should not be included with MREL in Iceland. Financial institutions in Iceland are still required to satisfy the combined capital buffer requirement and are not permitted to include CET1 capital with MREL, even though CET1 is used to satisfy the combined capital buffer requirement. With this approach, the flexibility provided for in the current MREL methodology under BRRD I is used to lay the foundations for the implementation of the MREL methodology under BRRD II. This approach should also ensure that capital accumulated for capital buffers will not be "locked in" with MREL; instead, it should be possible to use such capital to cover losses. There is doubt about whether this is realistic, however. Financial institutions are therefore required to calculate the loss absorption amount – and therefore the overall MREL requirement – excluding the combined capital buffer requirement currently in effect. Financial institutions are also notified of their MREL requirements without the combined capital buffer requirement and must make plans to satisfy the latter alongside the MREL.

4.2.2. Recapitalisation amount

The recapitalisation amount is based on a financial institution's capital requirement after the application of the preferred resolution action. The default recapitalisation amount is the minimum own funds requirement (Pillar I and Pillar II-R). To that amount it is possible to add a market confidence charge that is equivalent to the combined capital buffer requirement less the countercyclical capital buffer value. The Central Bank Resolution Authority is authorised to raise or lower the recapitalisation amount, both the default portion and the combined capital buffer requirement excluding the countercyclical capital buffer value; cf. Article 10, Paragraphs 5-8 of the MREL Regulation. The Resolution Authority's position is to leave the default amount unchanged; i.e., equal to the minimum own funds requirement. The Resolution Authority's position on the market confidence charge is covered in Section 5.3.

In determining MREL requirements, the proportional recapitalisation amount will be set based on the latest data on the institution's risk-weighted assets. On the other hand, the Resolution Authority will, as applicable, adjust the value of risk-weighted assets in its determination of the proportional recapitalisation amount, cf. Article 10, Paragraph 5(a) of the MREL Regulation, so as to reflect the institution's probable balance sheet position when it is failing or likely to fail. When an institution fails, it is likely that measures taken, such as remedial actions and other measures outlined in recovery plans, will have the effect of shrinking the institution's balance sheet. It is also likely that loan losses will affect a financial institution's balance sheet, particularly when credit risk is prominent in its activities. The greater the weight of credit risk in a financial institution's own funds requirements, the greater the likelihood that the recapitalisation amount will be adjusted. Adjustment of risk-weighted assets is limited to an amount equal to the total own funds requirement, and it should never exceed 10% of total assets. The Resolution Authority determines this adjustment of the recapitalisation amount in each specific instance.

The Central Bank Resolution Authority does not require that the recapitalisation amount be satisfied with specific liabilities other than CET1 or other capital instruments that the financial institution holds in excess of total required own funds. Therefore, institutions can use CET1 or other capital instruments in excess of minimum own funds requirements and capital buffers to satisfy requirements relating to the recapitalisation amount. On the other hand, financial institutions must consider the need to issue new liabilities or take other measures so as to have sufficient eligible liabilities to satisfy MREL requirements, particularly if they draw down their CET1 capital or other capital instruments in excess of the aforementioned requirements.

4.3. Position on the market confidence charge

As is provided for in Article 10, Paragraphs 6 and 7 of the MREL Regulation, a charge to ensure market confidence after resolution shall be part of the recapitalisation amount if the resolution authorities consider it necessary. This amount shall generally be equal to the combined capital buffer requirement less the countercyclical capital buffer value. It can be lower or higher, however; cf. Article 10, Paragraph 8 of the MREL Regulation.

The Central Bank Resolution Authority's position is that there is no need at this time to levy a market confidence charge on Icelandic financial institutions. Icelandic financial institutions are already bound by stringent own funds requirements, and they all use the standardised approach to calculate risk-weighted assets. One result of this is that their leverage ratios are high in comparison with peer credit institutions abroad – in the Nordic countries, for instance. Given Icelandic credit institutions' current funding and position, it is not deemed necessary to levy a market confidence charge.

The Resolution Authority's MREL Policy is updated on a regular basis, and at least every three years. When the next update is made, the Authority will review its position on the market confidence charge. The Resolution Authority will also review this position as it deems such review warranted; for instance, in the event of a change in Icelandic financial institutions' own funds requirements or funding, or in the event of material changes in their business model or risk profile, including increased activity in other EEA member states.

4.4. Position on subordination and eligible liabilities

In general, MREL requirements comprise, on the one hand, the requirement that institutions hold a specified minimum proportion of own funds and eligible liabilities so as to ensure that the preferred resolution action will be successful if resolution takes place, and on the other hand, certain conditions pertaining to eligible liabilities. This section of the MREL Policy focuses on the requirements that will be made of eligible liabilities.

4.4.1. Subordination

Financial institutions that undergo resolution must satisfy a specified share of MREL requirements with subordinated instruments, cf. Section 4.2 above, as the objective of such requirements is to ensure that bail-in will proceed smoothly during resolution. Applying bail-in to liabilities could lead to legal action during resolution if it entails discrimination against creditors whose claims rank equally (pari passu) vis-à-vis those to which bail-in is applied. As a result, it is vital to ensure that the no creditor worse off rule (Sections 2.2 and 4.2) is followed during the bail-in process. The subordination requirement is intended to place limits on this risk.

Subordination requirements relating to MREL – i.e., that certain liabilities to be used in particular for bail-in must rank below liabilities excluded from MREL and bail-in – were harmonised across the EEA with the adoption of BRRD II. According to Article 17, Paragraph 4 of Act no. 70/2020, the Resolution Authority decides what portion of MREL shall be subordinated. Furthermore, important conditions for eligible liabilities follow from Articles 72a and 72b of the CRR, as well as the definitions in Act no. 70/2020. The Resolution Authority makes its determination with an eye to the position of each financial institution.

The Authority therefore stresses that Act no. 70/2020, the MREL Regulation, and the CRR provide for ways to grant financial institutions flexibility in satisfying subordination requirements. This flexibility lies both in authorisations to extend deadlines for individual institutions and in provisions allowing for the inclusion of unsubordinated instruments in the subordinated portion of MREL requirements.

The former of these is provided for in Article 22 of the MREL Regulation, which authorises the Resolution Authority to grant extended deadlines to individual institutions. Further information can be found in Section 5.5 of this document. Among the factors the Authority considers in its decision on extended deadlines are developments in the relevant institution's financial position; expectations that the institution can ensure that it satisfies its MREL requirements within a suitable time frame; and whether the institution can swap out liabilities that do not satisfy subordination requirements, and if it cannot, whether this inability is limited to the entity itself or stems from market disruption.

The latter points are covered in Article 72b(3) and (4) of the CRR. Article 72b(3) authorises resolution authorities to permit the use of a specified maximum proportion of unsubordinated eligible liabilities (3.5% of risk-weighted assets) to satisfy MREL requirements, provided that they meet all of the criteria for eligible liabilities pursuant to Article 72b(1) of the CRR other than that they be subordinated to liabilities excluded from MREL and bail-in. Article 72b(4) authorises resolution authorities to permit financial institutions to include unsubordinated eligible liabilities with the subordinated portion of their MREL requirements, provided that they meet all of the criteria for eligible liabilities pursuant to Article 72b(1) of the CRR, and insofar as excluded liabilities of equal rank do not constitute more than 5% of the institution's own funds and eligible liabilities.

Resolution authorities are only permitted to grant exemptions based on either Article 72b(3) or Article 72b(4) of the CRR. Financial institutions must apply to the Central Bank of Iceland Resolution Authority for such exemptions. Exemptions may be granted only if all of the conditions in Article 72b(4) or Article 72b(4) of the CRR are satisfied, including the requirement that such an exemption may not create the risk that the no creditor worse off rule will be violated.

4.4.2. MREL at the group level

The financial instruments of a consolidated financial institution will be used to satisfy group-level MREL; cf. Article 18 of Act no. 70/2020. It should be noted, however, that CET1 capital held for capital buffers is not used to satisfy MREL requirements in Iceland, as capital buffers are not part of the loss absorption amount. Because the Resolution Authority's MREL Policy is based on a single point of entry approach, the Authority will only consider as eligible liabilities those financial instruments that are issued by financial institutions' parent companies, not those issued by subsidiaries. If a financial institution's liabilities are owned by its subsidiaries or affiliates, they cannot be classified as eligible liabilities; cf. Article 72b(2)(b) of the CRR.

4.4.3. Restrictions on cross-ownership

The BRRD framework assumes that risk stemming from cross-ownership of eligible liabilities should be restricted, in part because of the potential for contagion. The Central Bank Resolution Authority is tasked, for instance, with examining the types of owners of liabilities when preparing resolvability assessments, so as to determine whether cross-ownership of eligible liabilities exists. If it is revealed that such cross-ownership impedes resolvability, the Resolution Authority may respond by demanding that the institution sell specified assets or that it limit its portfolio of large exposures, both vis-à-vis specific parties and in the aggregate.

4.4.4. Other points regarding eligible liabilities for MREL

- Financial institutions are prohibited from exercising call options or retiring eligible liabilities before maturity without prior approval from the Central Bank Resolution Authority. The Authority shall authorise financial institutions to exercise call options or retire eligible liabilities if the conditions laid down in Article 78a(1) of the CRR are satisfied; cf. Section 6.2.
- If eligible liabilities contain incentives to call in or retire liabilities before maturity (step-up provisions), the assessment of whether the liability is considered qualified and eligible is based on the date such provisions first become exercisable, not the final maturity date; cf. Article 72c of the CRR.

- Liabilities cannot be considered eligible if they contain explicit or embedded derivatives. If such liabilities only contain call and/or put options, this does not prevent them from inclusion with MREL.
- Liabilities with set-off or netting provisions cannot be included with MREL if such provisions would prevent the financial institution from absorbing losses during resolution; cf. Article 72b(2)(f) of the CRR.
- When liabilities are issued outside the EEA, the financial institution must ensure that the terms and conditions of the issue include the counterparty's acknowledgement that the liability could be subject to bail-in and could therefore be used for recapitalisation during resolution, in accordance with Article 23 of Act no. 70/2020.
- The Resolution Authority stresses that it is the financial institution's responsibility to ensure that liabilities and equity instruments to be included with MREL satisfy all of the conditions necessary for consideration as eligible liabilities.

4.5. Deadlines for satisfaction of MREL requirements

The Resolution Authority is authorised to grant financial institutions a transition period to satisfy MREL requirements; cf. Article 22 of the MREL Regulation. According to the Temporary Provision in the MREL Regulation, the general deadline for satisfaction of subordination requirements in Iceland is 1 August 2026. Until then, the Resolution Authority will take decisions on subordination in connection with MREL. However, if a financial institution does not satisfy the subordination requirement according to the Authority's decision, the Authority will not restrict distributions in accordance with M-MDA rules; nor will it impose restrictions due to other impediments to resolvability, levy administrative fines under Act no. 70/2020, or apply other such onerous measures. Furthermore, the deadline for satisfying minimum requirements concerning subordination of own funds and eligible liabilities on the basis of Article 11 of the MREL Regulation (13.5% of risk-weighted assets, plus the combined buffer requirement) is set at three years from the date the minimum requirements are decided. The Resolution Authority emphasises, however, that it is always permissible to apply the specified measures due to general MREL requirements during the above-mentioned periods.

Moreover, the Resolution Authority is authorised to grant extensions beyond the aforementioned deadlines, based on the position of each institution and upon receiving an application from the institution concerned. If the Authority grants one or more such extensions, these are determined with an eye to the criteria laid down in Article 22 of the MREL Regulation. If this authorisation is exercised, the Resolution Authority will also inform the institution in question what the proposed MREL value will be once the extended deadline has passed, including what requirements must be satisfied within twelve months of the MREL decision.

The Resolution Authority encourages financial institutions in Iceland to give timely consideration to whether issuance of senior non-preferred securities is favourable and compatible with their institution's funding composition. The Authority also wishes to point out the exemptions under Article 72b(3) and (4) of the CRR, which authorise the inclusion of unsubordinated eligible liabilities with the subordinated portion of MREL (such as senior preferred debt instruments); cf. Section 5.4.1 above. It should be noted that the Resolution Authority will only be able to grant an exemption based on one of the two provisions.

4.6. Summary of MREL requirements

The Central Bank of Iceland Resolution Authority's MREL requirements are summarised below:

- The Resolution Authority will not adjust the default loss absorption amount. Therefore, the loss absorption amount will be equivalent to minimum required own funds (Pillar I and Pillar II-R).
- The loss absorption amount – and therefore the overall MREL requirement – are published excluding the combined capital buffer requirement currently in effect. Financial institutions must satisfy this requirement in tandem with the MREL.

- At the present time, the Resolution Authority will not adjust the default recapitalisation amount, which will be equivalent to the minimum own funds requirement.
- At the present time, no market confidence charge (MCC) will be levied in Iceland.
- The value of risk-weighted assets upon calculation of the proportional recapitalisation amount may be adjusted (reduced) based on the probable balance sheet position of the financial institution when it is failing or likely to fail.
- It is permissible to satisfy the recapitalisation amount using common equity Tier 1 capital or other capital instruments in excess of total required own funds.
- When an assessment is made of whether a financial institution satisfies weighted MREL requirements, it is prohibited to include common Tier 1 capital that is held in order to satisfy capital buffer requirements.
- Financial institutions in Iceland are required to satisfy requirements for eligible liabilities in accordance with the CRR.
- The Resolution Authority takes a decision on minimum subordination requirements for eligible liabilities, and financial institutions have until at least 1 August 2026 to satisfy these requirements in accordance with the MREL Regulation.
- The Authority is authorised to grant financial institutions a separate deadline or an extended deadline based on the position of the institution concerned; furthermore, it is possible to receive an exemption for inclusion of unsubordinated instruments with MREL requirements; cf. Article 72b(3) and (4) of the CRR.

5

Other MREL-related matters

Since the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, entered into force, the Resolution Authority has received a number of queries regarding MREL and has provided information in response to them. The Central Bank Resolution Authority's MREL Policy contains information relating to those queries that are deemed to have general significance and applicability to financial institutions in Iceland. In addition to the topics discussed in Sections 2-5 above, queries have been submitted regarding MREL-related transparency requirements, exemptions, and prior permission from the Authority to reduce eligible liabilities.

5.1. Publication of information on MREL

The Resolution Authority intends to disclose MREL-related decisions and requirements only to the financial institutions affected by them. Until 1 August 2026, financial institutions are free to disclose MREL-related information if they so choose. After that deadline, financial institutions will be required to publish, on a regular basis, information according to Annexes V and VI of Commission Implementing Regulation (EU) 2021/763, which has been implemented with the adoption of Rules no. 800/2024.

5.2. Prior permission from the Resolution Authority to reduce eligible liabilities

If a financial institution intends to call in, retire, repay, or repurchase instruments classified as eligible liabilities prior to their maturity date, it must apply to the Resolution Authority in advance for permission to take such action, pursuant to Article 78a of the CRR. The Resolution Authority handles such cases in accordance with Commission Delegated Regulation (EU) 2023/827 as regards the prior permission to reduce own funds and the requirements related to eligible liabilities instruments, particularly Articles 32a-32i of the Regulation. If a financial institution plans to reduce instruments included with eligible liabilities, the aforementioned application process begins with the submittal of a completed form that can be found on the Resolution Authority website.

5.3. Application for exemption from subordination requirements

Financial institutions that anticipate needing to avail themselves of either of the exemptions the Resolution Authority is empowered to grant in accordance with Article 72b(3) or (4) of the CRR must submit an application to the Authority. Applications for an exemption shall be sent to skilavald@sedlabanki.is with reference to the exemption provisions of the CRR.

5.4. Resolution-proof service agreements

The Resolution Authority reiterates that financial institutions must assess whether their service agreements are resolution-proof (i.e., whether they will retain their validity after resolution) and must update this assessment annually in the reports filed in connection with the preparation of resolution plans.