

CENTRAL BANK OF ICELAND



2024

# FINANCIAL SUPERVISION

One of the Central Bank of Iceland's most important tasks is to promote sound and secure financial activities.

The Central Bank monitors that the activities of supervised entities are in compliance with laws, regulations, rules, and company statutes governing such activities, and that they are consistent with sound and appropriate business practices. The objective of supervising financial activities is to promote a sound and secure financial market and to reduce the likelihood that the activities of supervised entities will result in losses for the general public.

The purposes of this report are:

- to explain how the Bank performs the tasks entrusted to it by law and how it followed its supervisory strategy and work timetable in the previous year;
- to provide information on the key supervisory priorities in the work timetable;
- to explain recent and forthcoming changes in the regulatory framework for the financial market.

In publishing this report, the Central Bank also attempts to ensure an appropriate level of transparency about its work and priorities in the field of financial supervision and to foster informed discourse about the financial system.

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**Symbols:**

- \* Preliminary or estimated data.
- 0 Less than half of the unit used.
- Nil.
- ... Not available.
- . Not applicable.

**Icelandic letters:**

ð/Ð (pronounced like th in English this)

þ/Þ (pronounced like th in English think)

In this report, ð is transliterated as d and þ as th in personal names, for consistency with international references, but otherwise the Icelandic letters are retained.

# The Central Bank's supervisory activities



This report describes how the Central Bank of Iceland followed its supervisory strategy and work timetable in 2023 by carrying out regular supervision and other monitoring. It also explains key financial system variables pertaining to the objective of promoting sound and secure operations among supervised entities.

## Supervision of financial undertakings, electronic money institutions, and payment institutions

The Central Bank supervises financial undertakings that have received operating licences pursuant to the Act on Financial Undertakings, no. 161/2002. On the one hand, it conducts regular supervision in accordance with its risk-based supervision model, and on the other hand, it conducts proactive checks based on current circumstances and risk assessments. The main focus of supervising financial undertakings' financial risk is to ensure that their capital and liquidity are strong enough to enable them to respond to unexpected shocks.

At the end of 2023, a total of 21 financial undertakings were subject to supervision by the Central Bank: four commercial banks, five savings banks, four credit undertakings, and eight investment firms. Also supervised by the Bank were two electronic money institutions, cf. the Act on the Issuance and Treatment of Electronic Money, no. 17/2013, and two payment institutions, cf. the Payment Services Act, no. 114/2021.

Three commercial banks – Arion Bank hf., Íslandsbanki hf., and Landsbankinn hf. – have been designated domestic systemically important banks (D-SIB) by the Central Bank Financial Stability Committee (FSN). These three banks together account for some

90% of total credit institution assets. Supervision of the systemically important banks is a wide-ranging task that involves conducting regular, systematic reviews of data on the banks' position, carrying out proactive checks and analyses, and taking interviews with selected senior managers and other key employees, as well as [external] auditors. Key metrics in the banks' operations are monitored, and an assessment is made of the sustainability of their business strategies and the viability of their business plans. In addition, various risks in their operations are examined and analysed on a regular basis – and more frequently if conditions warrant it.

### Supervisory review and evaluation process

Every year, the Bank's financial supervisors carry out a detailed supervisory review and evaluation process (SREP) on the four commercial banks. The SREP involves evaluating the viability and sustainability of the relevant undertaking's business strategy, governance practices, and internal controls, as well as assessing risks – credit risk, counterparty and concentration risk market risk, operational risk, and liquidity and funding risk – and conducting stress tests. In assessing these risks, the Bank uses the [Common procedures and methodologies for the supervisory review and evaluation process](#) (SREP Guidance). The SREP Guidelines were revised during the year and are based on the European Banking Authority (EBA) Guidelines on the same topic, which took effect on 1 January 2023 (EBA/GL/2022/03). A number of other guidelines were consulted as well.

The SREP reveals the efficacy of the mitigating measures adopted by the financial undertakings con-

cerned, whether its governance is sound and its capital base, and whether its liquidity and funding are adequate in view of the risks associated with its activities. During the SREP, the Bank also assesses and determines the banks' capital requirement under Pillar II-R, which indicates how much capital the bank in question must hold in view of the risks it faces or could face. The Pillar II-R capital requirement is in addition to the minimum capital requirement provided for under Pillar I.

For other financial undertakings, the SREP is carried out less often than for the commercial banks; i.e., generally every two to three years, unless circumstances call for greater frequency. In intervening years, less extensive annual risk analyses are carried out for these undertakings. This accords with the fundamental principle of risk-based supervision: that supervision should be broader in scope when it applies to undertakings that could jeopardise financial stability or expose a large group of customers to significant losses.

### **Monitoring of business models, credit risk, operational risk, governance practices, and internal controls**

#### **Business models**

The Central Bank analyses and assesses the viability of individual financial undertakings' business model and the sustainability of their business strategy. Legislative amendments enable existing and new financial market entities to offer technological solutions that have changed consumer behaviour and reduced the homogeneity of the banking market. The sustainability of financial undertakings' business strategies – i.e., their ability to generate acceptable return on equity over the medium term – has been a focal point of discussion in recent years. In 2023, particular emphasis was placed on assessing the impact of high interest rates on the viability of business models over the ensuing twelve months.

The commercial banks' operations have been generally successful, and profitability has increased. Interest income from lending has risen, partly because of loan portfolio growth and the impact of higher interest rates on variable-rate lending and liquid assets. Foreign funding terms have been volatile in the last couple of quarters. Competition is keen in the market for deposits, and depositors are now offered more favourable terms on special app-based or online bank-based accounts. Indexed term deposits with a commitment period of less than one year are also available. Financial undertakings' interest expense has therefore increased. In the recent past, financial undertakings and their customers have been faced with challenges

such as the global pandemic, wars and natural disasters, yet in spite of these headwinds, loans in arrears have not increased materially in the past year, as loan quality is high overall. Added to this is a demanding economic environment, with high inflation and interest rates. Higher debt service burdens have not resulted in increased arrears thus far but could do so in the future. The commercial banks' capital and liquidity ratios are well above regulatory requirements, which gives them considerable latitude to respond to increased arrears and loan losses.

Climate risk and the financial risk associated with it is a growing risk factor in financial undertakings' operations and will be given greater weight in the Central Bank's assessment of the sustainability of business strategies. The Central Bank has instructed the banks to incorporate international climate risk-related benchmarks and requirements into their business plans.

In the Bank's opinion, the viability and sustainability of the Icelandic commercial banks' business strategies is acceptable.

#### **Credit risk**

Priorities in supervision of credit risk have been shaped, among other things, by the scale of pandemic-related payment assistance measures, war, increased inflation, rising interest rates, and, most recently, the earthquakes and volcanic eruptions on the Reykjanes peninsula. In most cases, loans to borrowers who have taken advantage of mitigating measures are classified as forborne and performing, although this does not include general payment measures that are not necessarily due to debt service difficulties. The share of forborne loans has been falling, however, after peaking during the high point in the pandemic. Non-performing loan ratios have fallen as well and are low in historical context. They bottomed out in Q1/2023 and then rose marginally over the course of the year. There is still some uncertainty about recoveries on loans associated with the situation in the Reykjanes area. Loans granted to borrowers in the region account for 2% of total banking system lending, but a sizeable share of them are backed by collateral.

The regulatory framework for non-performing loans (NPL) has been strengthened substantially in recent years, in the wake of the European Commission's decision to embark on an initiative in response to a pent-up NPL problem in Europe. It is important that credit institutions adopt the new regulatory framework and follow the associated guidelines from the

European Banking Authority (EBA). The Central Bank considers it important that the credit institutions' framework for NPLs be satisfactory and that it enable the timely identification of risk, including the administration and recording of non-performing and forbore loans and a reliable assessment of loan impairment.

Icelandic credit institutions have little direct exposure in war zones. It is important that they monitor the impact that rising inflation and interest rates could have on households' and businesses' debt service capacity, and thereby on loan quality. Similarly, capital conservation buffers due to credit risk must reflect both short- and long-term risks.

### Operational risk

During the year, emphasis was placed on examining the overall framework and monitoring of operational risk in the financial market, with particular attention to the commercial banks. The Central Bank conducted on-site inspections focusing especially on determining whether the first line of defence was involved in preparing risk assessments, and whether the roles and responsibilities of the first and second lines of defence were in accordance with the EBA Guidelines on the supervisory review and evaluation process (SREP) and supervisory stress testing and the EBA Guidelines on internal governance. The Bank also examined operational risk assessments and adherence to related policy documents, processes, and procedures. In addition, the review of operational risk reports submitted to the Central Bank was examined and assessed.

In view of the Central Bank and the EBA's emphasis on cybersecurity, and given the growing threat stemming from cyberattacks, priority was given to strengthening the Bank's expertise in this field so that it will be better able to address cyber-related issues in coming years. Information security is a vast and complex topic that has relevance throughout much of Iceland's financial system, not least in the area of payment services. In H2/2023, the Central Bank began conducting appraisals of companies that provide payment services, with emphasis on examining their authentication procedures and their defences against fraud. The Bank's examination focuses in particular on whether the strong authentication requirements imposed by account servicing payment service providers (ASPSP) on payment initiation service providers (PISP) are fully in compliance with regulatory provisions. These appraisals will continue in 2024.

The forthcoming CRR III regulation amending Regulation (EU) no. 575/2013 (the CRR), which is set

to take effect in the EU on 1 January 2025, contains amendments to the approaches used by credit institutions to calculate their capital requirement relating to operational risk, and introduces a new standardised approach and replaces all current approaches. According to this new standardised approach, capital requirements will be based on operating income and historical losses due to operational risk; i.e., it will be assumed that operational risk varies directly with operating income and that estimated future losses due to operational risk will be in line with historical losses. The amendments entail a new methodology in which calculations are based, among other things, on specified business indicator component (BIC). The Central Bank will introduce these amendments once it becomes clear when they are to be implemented in Iceland.

### Governance and internal controls

The Central Bank analyses and assesses whether weaknesses in financial undertakings' governance and internal controls create risk and affect the undertakings' activities and sustainability. Emphasis is placed on assessing whether the governance structure ensures sound risk management and provides for appropriate internal controls in accordance with the three-lines model.

In its supervision of governance practices in 2023, the Bank assessed overall governance frameworks, including management structure and operations and the efficacy of the board of directors, with emphasis on how the board carries out its role in shaping the undertaking's risk culture. Financial undertakings' internal monitoring environment and the activities of their monitoring units were assessed as well. The assessment was based, among other things, on interviews with board members, managing directors, and heads of monitoring units, as well as on data gathered by the Bank. Following these assessments, the Bank made comments and recommendations where applicable and demanded remedial action.

The EBA Guidelines on the SREP and stress testing require monitoring of governance practices relating to environmental, social, and governance (ESG) risk and risks associated with anti-money laundering and terrorist financing (AML) measures. Weaknesses in the ESG and AML frameworks are therefore added to the tasks relating to internal controls and risk management in the assessment of financial undertakings' governance practices. The board's responsibilities in this context entail, among other things, setting priorities and ensuring that the aforementioned risks are part

of the overall framework for internal controls and risk management.

Implementation of the EBA Guidelines on sound remuneration policies began after amendments were made in 2022 to the provisions of the Act on Financial Undertakings on employment terms policies and bonus payments. The Bank also began preparing for the implementation of comparable European Securities and Markets Authority (ESMA) guidelines on employment terms in the securities market.

### **On-site inspections**

In 2023, continued emphasis was placed on on-site inspections relating to financial undertakings' credit risk. The Bank concluded inspections at Arion Bank hf. and Landsbankinn hf. pertaining to loan-to-value (LTV) and debt service-to-income (DSTI) ratios for consumer mortgages. The inspections involved an evaluation of lending procedures and processes, as well as a random sample check on compliance with Central Bank restrictions on such loans. A comparable inspection at Íslandsbanki hf. concluded in 2022. The results of the inspections at the three systemically important banks were published on the Central Bank website in May 2023.

During the year, on-site inspections were conducted at Arion Bank hf., Íslandsbanki hf., and Landsbankinn hf., with a focus on determining how the banks assessed and documented corporate loan collateral with respect to the provisions of Regulation (EU) no. 575/2013 (CRR). Related provisions in the EBA Guidelines on loan origination and monitoring and the EBA Guidelines on non-performing and forborne exposures were taken into account as well. Further on-site inspections relating to credit risk were also carried out in 2023 and were still ongoing at the year-end.

During the year, the Central Bank concluded on-site inspections at Arion Bank hf., Íslandsbanki hf., Kvika banki hf., and Landsbankinn hf., with the aim of examining operational risk frameworks and monitoring within various departments in the banks; i.e., whether roles and responsibilities according to the division of tasks among departments, on the one hand, and risk management, on the other, were in compliance with the Act on Financial Undertakings. Emphasis was placed on examining the operational risk assessments of the departments included in the inspection. Adherence to related policy documents, processes, and procedures was examined as well. The inspections also covered specified matters at the three systemically important banks in connection with their AML-related frameworks and division of tasks.

An on-site inspection focusing on outsourcing arrangements at Íslandsbanki hf. concluded in 2023 as well. Comparable inspections at Arion Bank hf. and Landsbankinn hf. concluded in 2022.

Moreover, on-site inspections were conducted at Arion Bank hf., Íslandsbanki hf., Kvika banki hf., and Landsbankinn hf., with the aim of determining how the banks satisfied requirements concerning management and monitoring of liquidity risk and funding risk.

Other on-site inspections carried out in 2023 centred on anti-money laundering and terrorist financing measures at Arion Bank hf., Íslandsbanki hf., Kvika banki hf., and the savings bank Sparisjóður Höfðhverfinga ses., as well as other supervised entities (discussed further on p. 27-28). The Bank also conducted on-site inspections focusing on the quality of trade reporting system (TRS II) notifications (discussed further on p. 24).

### **Recovery plans and resolution plans**

In the Central Bank's opinion, Icelandic credit institutions' recovery plans now satisfy the formal requirements made of them as regards contents and substance. The Bank has shifted its focus in its assessment of recovery plans, and now gives greater priority to analysing individual factors instead of conducting an overall assessment of the entire document. During the year, the Bank completed its assessment of recovery plans from Arion Bank hf., Íslandsbanki hf., Kvika banki hf., and Landsbankinn hf. In addition to general comments on substance and presentation, the Central Bank pointed out the importance of maintaining the contents of recovery plans so that they are always updated and ready for use, and are used as a good management tool in the banks' operations. Furthermore, the Central Bank requested that the commercial banks carry out appropriate appraisals and exercises in order to identify weaknesses and ensure effective, agile execution in the event that measures contained in the recovery plan need to be activated. It is also worth noting that the Central Bank has been updating its own contingency plans relating to credit institutions.

During the year, the Central Bank's Resolution Authority updated the resolution plans for the three systemically important banks. Concurrent with the update, the Authority also took decisions on the banks' minimum required own funds and eligible liabilities (MREL) pursuant to the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020, and the Bank's MREL Policy.



## Results of the IMF appraisal of the Central Bank's compliance with BCS Core Principles

The Basel Committee on Banking Supervision's (BCBS) Core Principles for Effective Banking Supervision were first issued in 1997 and then revised in 2012. In May 2023, another revision was circulated for a consultation process that concluded in October 2023. The final version has not yet been published, however.

In 2014 (prior to the 2020 merger between the Central Bank and the Financial Supervisory Authority), the International Monetary Fund (IMF) conducted an appraisal of the Icelandic Financial Supervisory Authority's compliance with the 2012 version of the Core Principles. Four non-numerical scores were given: compliant, largely compliant, materially non-compliant, and non-compliant.

Table 1 IMF scores in 2014 and 2023

|                          | 2014 | 2023 |
|--------------------------|------|------|
| Compliant                | 7    | 9    |
| Largely compliant        | 9    | 14   |
| Materially non-compliant | 13   | 6    |
| Non-compliant            | 0    | 0    |
| Total                    | 29   | 29   |

In the 2014 appraisal, the IMF found that the Financial Supervisory Authority was largely or fully compliant with 55% of the principles, but for the other 45% it was materially non-compliant. In the wake of this outcome, the Financial Supervisory Authority embarked on a major initiative to improve the areas considered unsatisfactory.

In 2022, the Icelandic authorities invited the IMF to conduct a comprehensive appraisal of the Icelandic

financial system under its Financial Sector Assessment Program (FSAP). The purpose of the FSAP appraisal was to determine the resilience of the financial system, the quality of the regulatory and supervisory framework, and the ability to respond to financial shocks. The appraisal included compliance with the 2012 BCBS Core Principles, the same version as in the Fund's 2014 appraisal. The IMF completed the appraisal in June 2023, and its findings were published in their entirety on the Central Bank website in July 2023. The table below summarises the results of the appraisal of compliance with the Core Principles:

In the 2023 appraisal, the IMF found that the Central Bank was largely or fully compliant with 79% of the principles but was materially non-compliant with the other 21%. As these figures show, the Bank has made significant progress in compliance with the Principles since the 2014 appraisal.

It is also appropriate to note that the IMF did not find the Bank fully compliant with certain Core Principles even though it was fully compliant with requirements under European law, as the Core Principles are not entirely aligned with the European regulatory framework. These perspectives from the Fund also apply to scoring of other European Economic Area (EEA) countries that have undergone IMF appraisals.

The Central Bank will continue to improve its compliance in areas deemed less than satisfactory by the IMF.

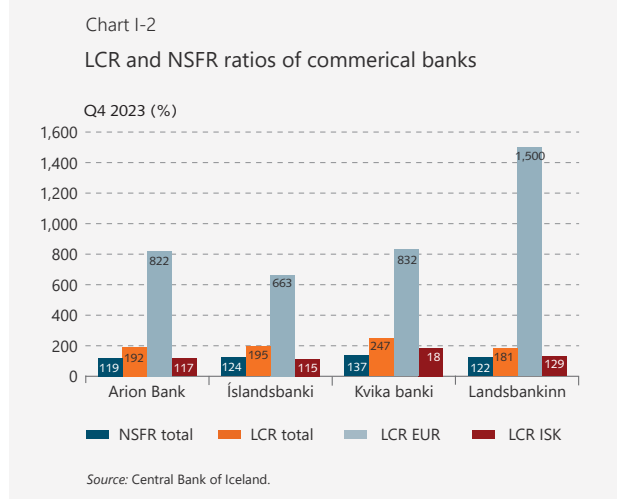
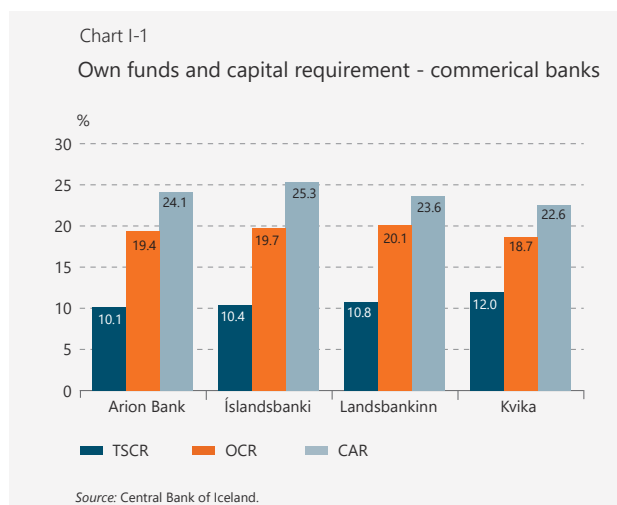
### Capital and liquidity requirements

On 15 March 2023, the Central Bank's Financial Stability Committee (FSN) decided to increase the countercyclical capital buffer (CCyB) value to 2.5%, whereas it had previously been set at 2% of domestic exposures. The FSN was of the view that the countercyclical capital buffer is an important element in banking system resilience. It was also of the opinion that increasing the CCyB was conducive to bolstering that resilience still further in the face of the risks that have accumulated and could materialise in the coming term. The new CCyB rate takes effect on 15 March 2024.

In July 2023, the Central Bank published the SREP results for Arion Bank hf., Íslandsbanki hf., and Landsbankinn hf. concerning additional capital requirements over and above minimum required own funds and the combined capital buffer requirement. The additional capital requirement for systemically important banks lay in the 2.1-2.8% range, bringing the overall capital requirement to 19.4-20.1% on a consolidated level.

In July 2023, SREP results for Kvika banki hf. concerning additional capital requirements were published as well. The additional capital requirement for the bank

was 4% and the overall capital requirement at the consolidated level 18.7%.

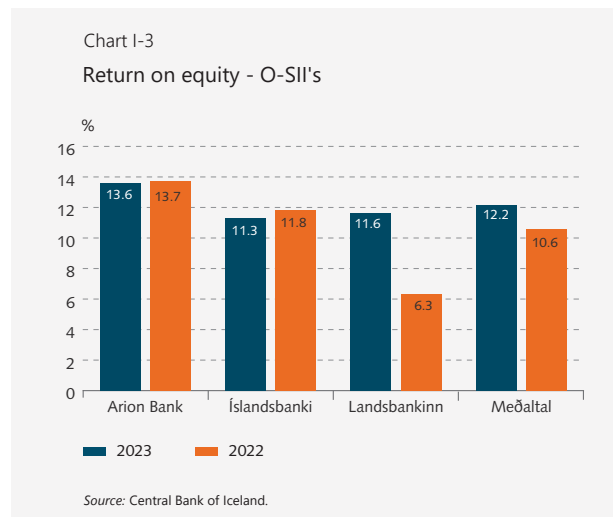


Liquidity and funding requirements according to the Rules on Credit Institutions' Liquidity Ratios, no. 1520/2022, are as follows: 100% liquidity ratio for all currencies combined, 80% for euros if euro-denominated obligations equal or exceed 10% of total obligations, 50% liquidity ratio in Icelandic krónur, and 100% funding ratio in all currencies combined. No additional liquidity or funding requirements were imposed on deposit institutions in 2023, as their liquid assets exceeded minimum requirements by 395 b.kr. at the end of the year.

### Systemically important banks' operating results

The systemically important banks' overall operating performance was good in 2023. Their combined after-tax profit totalled 83.5 b.kr., which represents a marked improvement relative to the prior year's 67 b.kr. Their

return on equity averaged 12.2%<sup>[1]</sup> in 2023, as opposed to 10.6% in 2022. Their returns on core operations were quite satisfactory and improved from the prior year. Their net interest income rose overall, and their average cost ratios declined year-on-year.



### Climate risk management - for financial undertakings

Climate risk – i.e., the financial risk attributable to climate change and responses to it – is one of the risks facing financial undertakings. The Central Bank monitors the assessment and management of such risk, largely through its regular SREP appraisals. In the 2023 SREP, the Bank conducted its first appraisal of the four commercial banks' climate risk and risk management, with reference to the BCBS Principles for the effective management and supervision of climate-related risks.

### Highlights

The banks have some knowledge of the topic and, in general, have set policies addressing climate risk. The result of this first appraisal was that adequate measures had been put in place in this area but that individual parties' responsibilities had yet to be defined fully. Furthermore, the assessment of the banks placed considerable emphasis on their impact on their environment as compared with the risks they themselves face. These two are often combined as well.

The banks' internal audit departments generally have limited involvement in monitoring climate risk. Such monitoring is largely in the hands of risk management departments, although work is being done to increase the involvement of front-line staff and those who take lending decisions.

The banks' analysis of climate risk is relatively rough overall, and largely entails acknowledging that

such risk exists. In general, no material risk factors have been identified that could cause significant losses, nor has the risk appetite relating to such factors been defined. The factor that comes closest to being classified as a risk is ocean acidification, which some of the banks believe could negatively affect the fishing sector, but not enough to necessitate a defined risk appetite. The climate risk metrics set forth by the banks are limited, apart from financed emissions as a measure of the cost of emissions, which the banks commonly calculate. Nevertheless, the banks have set targets for “green” financing, and it can be assumed that climate change will have less negative impact on loans of this type.

To some extent, the banks assess the climate risk associated with new lending, but they have not yet assessed the impact of climate risk on individual risk factors. Furthermore, capital requirements due to cli-

mate risk either have not been assessed or are deemed not to exist.

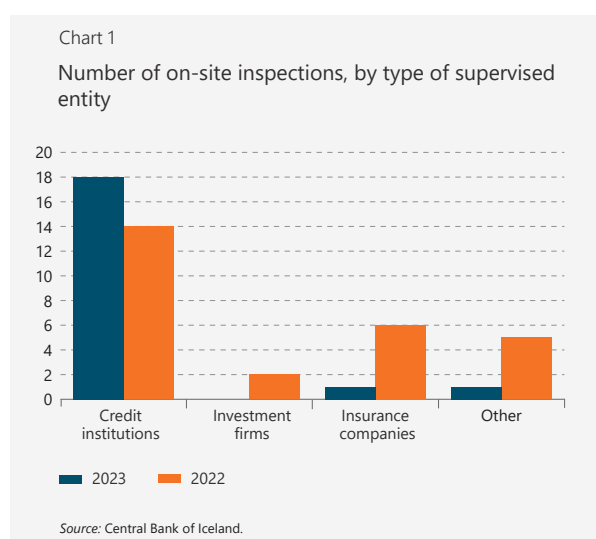
The banks’ boards of directors receive regular information on climate risk, but in their opinion, this information is unsatisfactory due to a shortage of data and the lack of a harmonised methodology.

### Comments and recommendations

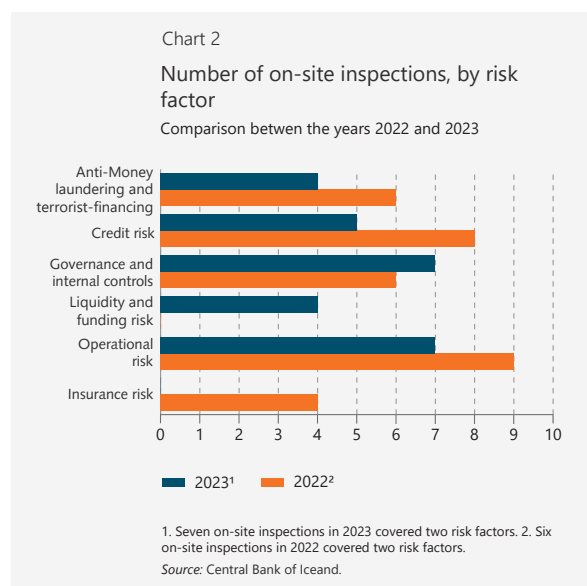
Pursuant to the information given by the banks on their monitoring of climate risk, they were encouraged to analyse climate risk in greater detail than before, in order to identify important risk factors that need to be managed. A part of this management would be to develop a set of risk indicators, which would serve as metrics for the risks identified, and to set boundaries for those risk indicators that would reflect the banks’ risk appetite. For example, the cost of emissions (pur-

## On-site inspections

On-site inspections support regular ongoing supervision of supervised entities. They are one of the methods the Central Bank uses to carry out its legally mandated role of reviewing and assessing underlying risks in supervised entities’ activities and evaluating their governance practices and frameworks for internal controls. Decisions about on-site inspections are based on the supervised entity’s impact category and the results of risk assessments. Consideration is also given to the nature, size, systemic importance, and complexity of the entity’s activities.



The Central Bank completed 20 on-site inspections in 2023, as compared with 27 in 2022. As is noted above, continued emphasis was placed on assessing supervised entities’ AML measures, as well as carrying out checks on credit risk, operational risk, liquidity and funding risk, governance practices, and internal controls in supervised entities’ activities.



chase of fuel fossils and possible levies on emissions) could be defined as a risk for which financed emissions would be a risk indicator.

The banks were also encouraged to distinguish more clearly between the environmental risks stemming from their activities and the environmental risk they themselves face, and to address the risk they face specifically.

### The next steps

The banks are beginning to work on climate risk management. The first step is to identify the risk that must be managed. Even though it has been acknowledged that climate change creates risk for the banks, no well-defined material risk factors have yet been identified in this context. In view of this situation, the Central Bank emphasises that the banks should strengthen their risk analysis methodology.

Climate risk management will evolve in the coming term. With the identification of better-defined risk factors, the methodology for assessing these risks will become clearer, both for the banks and for the Central Bank. This is a process that will take time and will probably never be truly complete.

### European cooperation

Cooperation with the EBA affects regular supervision of financial market entities, as issues emphasised by the EBA are reflected in the Central Bank's supervisory timetable. Furthermore, the EBA plays a crucial role in shaping the regulatory framework for financial institutions in the EEA, and the Central Bank monitors this work closely, including by participating in various working groups and committees. The Bank also engages in various types of institutional cooperation with its Nordic and Baltic neighbours.

## Supervision of insurance activities

The Central Bank supervises insurance companies that have received operating licences pursuant to the Act on Insurance Activities, no. 100/2016. This supervision entails, on the one hand, regular monitoring in accordance with the Bank's risk-based supervision model, which defines the frequency with which key risk factors in the companies' operations are examined, and on the other hand, proactive checks carried out based on the Bank's priorities and the circumstances in each given instance. The Bank analyses key risks and developments in the markets; furthermore, it conducts monitoring to ensure that the entities concerned satisfy the require-

ments for their operating licences, that their operating practices are in compliance with regulatory provisions, and that appropriate measures are taken at all times. Furthermore, the Bank supervises the activities of insurance brokerages and monitors the business conduct of foreign insurers licensed to do business in Iceland.

At the end of 2023, four non-life insurance undertakings and four life insurance undertakings were operating in Iceland on the basis of operating licences issued by the Central Bank. Also in operation was one reinsurance undertaking engaged in the settlement of run-off obligations, as well as The National Catastrophe insurance provider NTÍ, a Government institution operating under special legislation. Nine insurance brokerages have been licensed by the Central Bank, and a number of insurers and brokers in the European Economic Area (EEA) have submitted notifications of activities in Iceland.

### Ongoing supervision

Ongoing supervision of insurance undertakings centres on their solvency position and their ability to cover financial obligations. The Central Bank reviews regularly submitted reports and takes interviews with CEOs, persons responsible for key functions, and external auditors. Furthermore, the Bank carries out an annual assessment of risks relating to insurance companies' operations in accordance with its [General criteria and methodology for supervision of insurance companies](#). Cooperation with the European Insurance and Occupational Pensions Authority (EIOPA) is an important aspect of ongoing supervision of insurance undertakings. EIOPA's priorities are reflected in the Central Bank's supervisory timetable, for example, and EIOPA organizes the supervisory priorities and common supervisory practices in the insurance market.

In 2023, emphasis was placed on the quality of data in regular filings and on the premises for calculating solvency capital requirements according to the standardised formula. In some instances, comments were made on the calculations and corrections were requested. The Central Bank emphasises strongly that insurance companies have in place systems and organisational structures that ensure data quality and reliability.

### Seismic activity on the Reykjanes peninsula

The Central Bank examined the responses of domestic insurance undertakings during the prelude to the declaration of emergency in Grindavík and the evacuation of the town in November 2023. The insurance com-

panies were in contact with policyholders in the area and provided them in some cases guidance aimed at updating the insured value of their personal belongings so as to gain a better overview of potential losses. Shortly afterwards, Natural Catastrophe Insurance of Iceland (NTÍ) issued an announcement prohibiting new insurance contracts or amendments to existing ones, as an insured event had already begun or was imminent; cf. Article 6 of the Regulation on Natural Catastrophe Insurance of Iceland, no. 770/2023.

NTÍ's role is to insure against damage caused by natural disasters. It is mandatory to insure all buildings and liquid assets that are insured against fire by a general insurance undertaking, as well as specific structures that may not be fire-insured, such as district heating and harbour structures. By law, NTÍ covers only losses directly attributable to natural disasters, not indirect losses. As a result, liability in cases of natural disasters usually falls outside the coverage of other general insurers' terms and conditions; for instance, coverage of an business interruption insurance generally excludes natural disasters unless the policy contains specific provisions to the contrary.

### **Changes in financial reporting**

According to the Act on Insurance Activities, insurance undertakings' annual accounts are prepared in accordance with international financial reporting standards. A new international reporting standard, IFRS 17 Insurance Contracts went into force in 2023, replacing the previous IFRS 4. The new standard provides for changes in presentation of both profit and loss accounts and balance sheets, as well as requiring more detailed disclosure requirements

### **Changes in insurance companies' data filings**

Changes in data filings submitted by insurance undertakings operating in the EEA took effect at the end of 2023. Since the Act on Insurance Activities entered into force in accordance with the EU Solvency II directive, regulatory reporting for insurance undertakings' within the EEA has been harmonised. In accordance with a new implementing regulation, insurance undertakings must also provide information on climate risk and cyber risk for non-life insurance.

### **Operational risk**

During the year, three thematic on-site inspections focusing on operational risk were carried out at insurance undertakings. The inspections centred on procedures and processes relating to policies on operational risk,

the outsourcing framework, the contingency framework, cloud services, and information technology. Two of these inspections were still ongoing at the end of 2023.

### **Operations of foreign controlled insurance undertakings**

Insurance undertakings headquartered in other EEA member states are authorised to sell insurance and reinsurance policies in Iceland, either through right of establishment or freedom to provide services. A number of foreign insurers have notified the provision of service in Iceland through freedom to provide services. Most of the premiums paid to foreign insurance undertakings are due to the purchase of foreign life insurance policies and other life and health insurance policies. Information on sales made in Iceland by insurance undertakings licensed in other EEA states is gathered through EIOPA. Foreign insurance companies' recognised premiums totalled 26.9 b.kr. in 2022. The majority of these premiums were for the purchase of foreign life insurance policies (18.3 b.kr.), while premiums for other life and health insurance totalled 318.7 m.kr. The total amount of premiums in 2023 is not yet available. Premiums for pension insurance are paid mainly to foreign life insurance companies that offer supplemental insurance protection on the basis of Article 8 of the Act on Mandatory Insurance of Pension Rights and on Activities of Pension Funds, no. 129/1997.

## **Supervision of pension funds and third-pillar pension providers**

The Central Bank supervises pension funds and third-pillar personal pension providers. This entails, on the one hand, regular ongoing monitoring in accordance with the Bank's risk-based supervision model, which defines the frequency with which key risk factors in the pension funds' operations are examined, and on the other hand, proactive checks carried out based on the circumstances and reasons prevailing in each given instance. Key risks and developments in the market are examined. The Bank monitors to ensure that the entities concerned satisfy the requirements for their operating licences, that their operating practices are in compliance with regulatory provisions, and that appropriate measures are taken at all times. Furthermore, the pension funds' risk assessments are examined, and interviews are taken with selected key employees.

In 2023, a total of 21 pension funds accepted mandatory pension contributions in collective pension-schemes, and 13 of them offered voluntary third-pillar

## Suitability assessments

The Central Bank assesses the suitability and qualifications of supervised entities' board members and managing directors. Suitability assessments are conducted when board members and managing directors begin work for supervised entities. In addition, the Central Bank may conduct a reassessment if warranted. However, the entities concerned are always responsible for ensuring that their board members and managing directors satisfy the regulatory eligibility requirements in place at any given time.

During the assessment, submitted documents are evaluated, and in a large number of instances, board members are interviewed and their expertise examined more thoroughly. In determining whether a board member should be interviewed, consideration is given to factors such as the type, size, and scope of the supervised entity's operations, and whether there is any doubt about whether the person concerned meets the regulatory requirements concerning the expertise, qualifications, and experience needed to fulfil their role in a satisfactory manner. In the case of managing directors, a thorough verbal assessment of the person's expertise is always carried out, and written documents are evaluated as well.

**Table 1 Suitability assessments of board members and managing directors 2023**

| Type of supervised entity                 | Number |
|---|--------|
| Commercial bank                           | 9      |
| Credit undertaking                        | 17     |
| Investment firm                           | 8      |
| Payment institution                       | 13     |
| Electronic money institution              | 1      |
| UCITS management company                  | 4      |
| Alternative investment management company | 11     |
| Insurance company                         | 12     |
| Pension fund                              | 25     |
| Total                                     | 100    |

**Table 2 Suitability assessments of board members and managing directors 2021-2023**

|   | 2021 | 2022 | 2023 |
|---|------|------|------|
| Number of individuals assessed  | 94   | 97   | 100  |
| Number of individuals who did not pass due to insufficient knowledge or failure to appear for interview | 2    | 2    | 4    |

The Central Bank assessed the suitability of 100 board members and managing directors in 2023. Of these, four either did not pass the assessment due to inadequate

expertise or failed to appear for the interview. As in previous years, most of the assessments involved board members.

### Qualifying holdings and control

The Central Bank assesses the eligibility of parties intending to acquire qualifying holdings in supervised entities. A qualifying holding is a direct or indirect holding in a supervised entity amounting to 10% or more of its share capital, guarantee capital, or voting rights, or another holding that enables the exercise of significant influence on the management of the entity concerned.

In 2023, the Bank processed notifications of qualifying holdings in 14 supervised entities, two of which were notifications involving two entities. In addition, one notification of control over a supervised entity was processed.

The companies Dalgeiri ehf. and Misgengi ehf. and parties related to them were deemed eligible to own a qualifying holding in Ísafold Capital Partners hf., cf. the Act on Alternative Investment Fund Management Companies, no. 45/2020. It was also concluded that the companies Bergholt eignir ehf., MC2 Invest ehf., and Mörk Capital ehf. and related parties were eligible to own a qualifying holding in Akta sjóðir hf.; cf. the Act on Alternative Investment Fund Management Companies. The Pension Fund of Commerce was deemed eligible to own a qualifying holding in insurance company Vátryggingafélag Íslands hf. and its subsidiary Líftryggingafélag Íslands hf.; cf. the Act on Insurance Activities, no. 100/2016. Fossar Investment Bank hf. and related parties were declared eligible to own a qualifying holding in T Plús hf.; cf. the Act on Markets in Financial Instruments, no. 115/2021. Vátryggingafélag Íslands hf. was declared eligible to own a qualifying holding in Fossar Investment Bank hf. and its subsidiaries and affiliates Glymur hf. and T Plús hf.; cf. the Act on Financial Undertakings, the Act on Alternative Investment Fund Management Companies, and the Act on Markets in Financial Instruments. Furthermore, it was concluded that the company Adenza Parent LP and related parties were eligible to own a qualifying holding in Nasdaq Iceland hf.; cf. the Act on Markets in Financial Instruments.

Moreover, the following notifications of qualifying holdings were processed in connection with the grant of a new operating licence. With the grant of an operating licence to Straumur greiðslumiðlun hf., Kvika banki hf. was

deemed eligible to own a qualifying holding in the company; cf. the Payment Services Act, no. 114/2021. Furthermore, with the grant of an operating licence to Glymur hf., it was concluded that Fossar Investment Bank hf. and related parties were eligible to own a qualifying holding in the company; cf. the Act on Alternative Investment Fund Management Companies. In connection with the grant of an operating licence to Blikk hugbúnaðarþjónusta hf., the company InfoCapital ehf. and related parties were deemed eligible to own a qualifying holding in the company; cf. the Payment Services Act. With the grant of an operating licence to SIV eignastýring hf., it was concluded that Vátryggingafélag Íslands hf. and the companies Maldini ehf., Salka2 ehf., and YNWA ehf. and related parties were eligible to own a qual-

ifying holding in the company; cf. the Act on Alternative Investment Fund Management Companies. In connection with the grant of an operating licence to A/F Rekstraraðili hf., securities firm Arctica Finance hf. and related parties were declared eligible to own a qualifying holding in the company; cf. the Act on Alternative Investment Fund Management Companies.

Furthermore, it was concluded that the company Inniðir fjárfestingar slhf. and related parties were eligible to exercise control of securities depository Verðbréfamiðstöð Íslands hf., cf. the Act on Central Securities Depositories and Settlement and Electronic Registration of Financial Instruments, no. 7/2020.

personal pension savings in 43 divisions. Also in operation were seven other third-pillar personal pension providers with a total of 33 divisions, plus two foreign insurance companies offering third-pillar pension savings.

### **Ongoing supervision**

Ongoing supervision of pension funds and third-pillar pension savings custodians entails monitoring their compliance with regulatory provisions and assessing the risk in their operations. The Central Bank assesses risks associated with pension funds' activities. These assessments are based in particular on information from regular data filings; interviews with managing directors, actuaries, risk officers, internal auditors, and board members; and the results of proactive supervisory checks.

### **Amendments to pension funds' Articles of Association**

According to Article 28 of the Act on Mandatory Insurance of Pension Rights and on Activities of Pension Funds, all amendments to pension funds' Articles of Association must be announced to the Minister, and they will not take effect until the Minister has confirmed, upon receiving a statement from the Central Bank, that they are in compliance with both statutory provisions and the provisions of the current Articles of Association for the pension fund concerned. In 2023, the Bank submitted statements on amendments to the Articles of Association for 15 pension funds. In several instances, the amendments involved a curtailment of pension rights resulting from results of the actuarial

examinations on the solvency position as of year-end 2022. In addition, several pension funds amended their provisions on minimum contributions and introduced specified private pension savings in accordance with statutory amendments.

### **Governance, operational risk, and outsourcing**

As in previous years, inspections of pension funds' governance practices played an important part in the Central Bank's supervisory activities in 2023. Emphasis was placed on risk culture, assessing board risk awareness, and analysing conflicts of interests, as well as examining pension funds' monitoring systems. Comments and recommendations were communicated where applicable following these checks.

Specified aspects of nine pension funds' operational risk were examined in 2023. The Bank requested an outsourcing register and conducted a random check of outsourcing agreements. In addition, it examined whether the pension funds in question monitored outsourced projects, and it gathered information on contingency plans and contingency testing.

### **Minimum pension requirements**

In 2023, the Central Bank sought a pension fund's opinion of whether the accrual of pension rights was sufficient to cover the minimum pension insurance protection required by law. The examination revealed that fund members did not accrue enough rights to cover minimum pension insurance protection, and the fund responded by making changes to rights accrual and raising the pension entitlement age.

### **Pension funds' sustainability journey**

The Central Bank began an appraisal of pension funds' sustainability risk management during the year. In this instance, the appraisal was limited to climate risk as a facet of sustainability risk. The funds' management of climate risk was examined, and comments and recommendations will be sent to them afterwards.

### **The IMF's FSAP appraisal of the Icelandic financial system**

As is noted above, the IMF conducted an appraisal of all major pillars of the Icelandic financial system in H1/2023. The IMF mission met with representatives from the Central Bank, Government ministries, and various stakeholders in the business community, including the pension funds. In the appraisal, the IMF placed particular emphasis on the Icelandic pension funds. The Fund's main conclusion was that the financial system was sufficiently resilient, but some weaknesses were revealed as well. The IMF was of the opinion that there were opportunities to strengthen the legislative framework for the pension market. In this context, it was proposed that governance requirements be tightened and supervision of pension funds be increased because of their systemic importance in the financial market.

### **Green paper and special report on pension issues**

The Central Bank met with a group tasked by the Minister of Finance and Economic Affairs with the preparation of a green paper on pension funds, whereupon it submitted three memoranda outlining its priorities and proposals for amendments to legislation on pension rights and pension funds. Some of these priorities and proposals were a summary of proposals previously highlighted by the Central Bank[ and, before its 2020 merger with the Bank, the Financial Supervisory Authority].

The Bank is also preparing to issue a special report (discussion paper) on the key points that it considers important to take into account in connection with future amendments to pension fund legislation.

### **Penalties**

In May 2023, the Pension Fund for State Employees agreed to settle a case involving the fund's violation of Article 58, Paragraph 1 of the Act on Insurance Activities, no. 100/2016, by failing to notify in advance its plans to acquire a direct qualifying holding in Vátryggingafélag Íslands hf. and an indirect qualifying holding in Líftryggingafélag Íslands hf. Under the settlement, the pension fund agreed to pay a fine of 2.5

m.kr. to the Treasury. The agreement was published on the Bank's website that same month.

## **Supervision of business conduct and consumer affairs**

The Central Bank carries out monitoring to ensure that the activities of supervised entities are consistent with sound and appropriate business practices. The Bank's objectives include promoting professionalism, fairness, and honesty in the provision of services in the financial market, with the aim of strengthening the protection of investors and consumers. The Bank conducts a number of investigations relating to business practices each year, both on its own initiative and pursuant to tips it receives. It has also analysed various aspects of investor conduct, such including an analysis of retail investors' investments and risk appetite.

The objectives of supervising business conduct include ensuring that supervised entities' activities are in compliance with regulatory provisions, with the aim of strengthening investor protection and bolstering confidence in the financial market. Business conduct includes supervised entities' information disclosures to customers, customer classification, record-keeping and storage of data (including telephone conversations), and handling of complaints. As a result, any type of communications that take place between a supervised entity and existing or potential customers and that pertain to the provision of investment service or investment activities may fall under the fundamental principles of business conduct.

In 2023, the Central Bank concluded various investigations relating to business conduct and consumer affairs. The Bank also continued its wide-ranging investigations of domestic managers and book runners in Icelandic State Financial Investments' spring 2022 offering of a 22.5% Government-owned stake in Íslandsbanki hf. Two investigations of the execution of the offering concluded during the year, one by settlement and the other with a transparency announcement. Other related investigations are still ongoing.

In 2023, the Central Bank strengthened its Conduct Supervision Department further by increasing staffing levels. This is in accordance with both the Bank's Supervisory Strategy and the priorities of the European Supervisory Authorities (EBA, EIOPA, and ESMA). The Central Bank is currently formulating a risk-oriented approach to supervision of business conduct, which is intended to focus the Bank's attention on work practices, weaknesses, and risks in the financial



## Licensing and related matters

One of the Central Bank's tasks is to process applications by businesses – and, in some instances, individuals – for licences to operate in the financial market. Such work can be broad in scope and requires the involvement of experts with wide-ranging knowledge. There were significant changes relating to supervised entities' operating licences and other permits in 2023:

- Fossar Investment Bank hf. was granted an expanded operating licence on the basis of the Act on Markets in Financial Instruments, no. 115/2021. The expanded authorisations include underwriting in connection with issuance and/or offering of financial instruments, and services in connection with underwriting.
- Straumur greiðslumiðlun hf. received a licence to operate as a payment institution on the basis of the Payment Services Act, no. 114/2021. The payment institution is authorised to execute payments, including transferring funds to and from a payment account with the user's payment service provider or another payment service provider, to execute payments if funds are guaranteed with a credit line for the user of payment services, and to issue payment instruments and/or act as acquirer for payments.
- Blikk hugbúnaðarþjónusta hf. was granted a licence to operate as a payment institution on the basis of the Payment Services Act. The payment institution is authorised to operate as a payment initiation service provider and an account information service provider.
- The electronic money institution Rapyd Europe hf. and the payment institution Valitor hf. merged; cf. the Act on the Issuance and Treatment of Electronic Money, no. 17/2013, and the Payment Services Act. The aforementioned company discontinued operation, and the latter took over all of its rights and obligations. The merged company now operates as an electronic money institution under the name Rapyd Europe hf.
- The investment firm ACRO verðbréf hf. received authorisation for nominee registration; cf. the Act on Markets in Financial Instruments.
- SIV eignastýring hf. was granted a licence to operate as an alternative investment fund manager; cf. the Act on

Alternative Investment Fund Management Companies, no. 45/2020. The licence authorises the company to operate alternative investment funds, engage in asset management activities, and receive and transmit orders pertaining to financial instruments.

- A/F Rekstraraðili hf. was granted a licence to operate as an alternative investment fund manager; cf. the Act on Alternative Investment Fund Management Companies. It had been registered as an alternative investment fund manager since 2021. The licence authorises the company to operate alternative investment funds.
- Glymur hf. was granted a licence to operate as an alternative investment fund manager; cf. the Act on Alternative Investment Fund Management Companies. It had been registered as an alternative investment fund manager since 2021. The licence authorises the company to operate alternative investment funds.
- The companies Aldir ehf., Founder Ventures Management ehf., MGMT Venture Capital ehf., Nordic Ignite ehf., ORCA Capital Partners ehf., and REC SJÓDIR ehf. were registered as alternative investment fund managers; cf. the Act on Alternative Investment Fund Management Companies. The registration provides for a limited authorisation to operate alternative investment funds.
- IsMynt ehf. was registered as a virtual currency service provider on the basis of the Act on Measures against Money Laundering and Terrorist Financing, no. 140/2018.

### Unauthorised operation of licensed activities

The Central Bank conducts proactive investigations and regularly receives tips on companies suspected of carrying out activities requiring licensing of registration without the required authorisations. In 2023, the Bank examined the activities of 33 parties, including 22 cases still pending from 2022. Of these cases, 31 were proactive checks and two resulted from tips received by the Bank. Investigations of 13 parties' activities are still ongoing and are set for completion in 2024.

market that could be damaging to consumers' and investors' interests.

### **Íslandsbanki hf. execution of the sale of the State's holding in the bank**

The Central Bank completed its investigation of Íslandsbanki hf. practices in connection with the 22 March 2022 sale by offering of a 22.5% Government-owned shares in the bank. The aim of the investigation was to determine whether the bank had fulfilled its obligations as joint global coordinator in the auction as laid down in the Act on Markets in Financial Instruments, no. 115/2021, cf. Commission Delegated Regulation (EU 2017/526, and the Act on Financial Undertakings, no. 161/2002. The investigation included the bank's provision of investment services and its governance practices. The Central Bank found that the bank had violated Article 10, Paragraphs 4 and 5; Article 21, Paragraphs 1 and 2; the first and second sentences of Article 23, Paragraph 2; Article 32, Paragraph 1; Article 33, Paragraph 1; Article 34, Paragraph 1; and Article 54, Paragraph 1 of the Act on Markets in Financial Instruments; Article 34(3)(a) of Commission Delegated Regulation 2017/565; cf. Articles 3 and 32 of the Act on Markets in Financial Instruments; Article 38(2) of Commission Delegated Regulation 2017/565; cf. Articles 3 and 32 of the Act on Markets in Financial Instruments; Article 41(2) of Commission Delegated Regulation 2017/565; cf. Articles 3 and 32 of the Act on Markets in Financial Instruments and Article 76(6) of Commission Delegated Regulation 2017/565; cf. Articles 3 and 23 [sic] of the Act on Markets in Financial Instruments; the then-current first sentence of Article 17, Paragraph 1 and Article 54, Paragraphs 1 and 3 of the Act on Financial Undertakings, no. 161/2002; cf. Article 10, Paragraph 3 of the Act on Markets in Financial Instruments; in that the board and CEO of Íslandsbanki hf. had failed to implement satisfactory governance and internal controls ensuring effective and prudent management. This had led, among other things, to the bank's failure to satisfy statutory requirements and comply with internal rules set by its board. Íslandsbanki hf. requested to conclude the matter by settlement. The Central Bank of Iceland decided to conclude the case with a settlement providing for the payment of a fine in the amount of 1.160 b.kr. and a pledge to implement reforms.

Among the violations described in the settlement are Íslandsbanki hf. failure to make audio recordings of telephone conversions, its provision of incorrect information to customers on the terms of offering,

and its failure to comply with statutory requirements in assessing customers' applications for classification as professional investors. Furthermore, the bank failed to take sufficient action to prevent conflicts of interests – such as measures relating to employee participation in the offering and adequate separation of departments within the organisation. The Central Bank concluded as well that the bank had not prepared a risk assessment in connection with its involvement in the sale process. Íslandsbanki hf. had also provided customers of its asset management department with incorrect and misleading information about minimum bid amounts in the offering and had provided Icelandic State Financial Investments with misleading information on the classification of investors participating in the offering and the means by which they were invited to participate. By inviting retail investors to participate in an offering intended solely for qualified investors, Íslandsbanki hf. did not comply with Icelandic State Financial Investments' terms of offering. Finally, in preparing and executing the offering, it was concluded that Íslandsbanki hf. did not satisfy in all respects its obligation to operate honestly, fairly, and professionally in accordance with appropriate and sound business practices, with the credibility of the financial market and the interests of its customers as guiding principles.

The settlement agreement was published on the Bank's website in June 2023.

### **Landsbankinn hf. execution of the offering held by Icelandic State Financial Investments**

The Central Bank completed its investigation of Landsbankinn hf. execution of the offering. The aim of the investigation was to determine whether, in the offering, the bank had fulfilled its obligations as provider of investment services as laid down in the Act on Markets in Financial Instruments, no. 115/2021. The investigation covered customer classification, documentation and storage of telephone conversations and other electronic communications, and measures to address conflicts of interests. The Central Bank found that Landsbankinn hf. was in violation of the Act on Markets in Financial Instruments in that it failed to carry out a satisfactory valuation of two customers' financial instruments when they requested classification as professional investors. Furthermore, the bank violated the same provision by accepting and entering bids from four customers who were classified as retail investors at the time the bids were received and entered, and by confirming the classification of two of them as professional investors before written applications for such

classification had been received by the bank. They were later classified as professional investors. In view of the nature and scope of the violations, the Central Bank did not consider it appropriate to impose penalties on the bank. Landsbankinn hf. immediately took action to rectify the matters outlined in the Central Bank's findings.

A transparency announcement about the case was published on the Central Bank website in December 2023.

### Information disclosure to customers of NOVIS

An investigation was conducted on amendments to the terms and conditions for NOVIS insurance policies before the company's operating licence was revoked by National Bank of Slovakia (NBS) in June 2023. The aim of the Central Bank's investigation was to determine whether the company satisfied requirements for information disclosures to policyholders in connection with amendments to terms and conditions pursuant to the Act on Insurance Activities, no. 100/2016, and the then-current Rules on Appropriate and Sound Business Practices of Insurance Undertakings, no. 673/2017 (now the Rules on Appropriate and Sound Business Practices,

Communications with Customers, and Handling of Complaints, no. 353/2022). The Central Bank concluded that NOVIS had provided policyholders in Iceland with misleading and deceptive information on amendments to complex terms and conditions for specified insurance-linked investment products. Because of this, it had been virtually impossible for policyholders to understand the significance of the amendments and make informed decisions on whether the amendments were in their best interests, as the amendments were made on the basis of tacit consent. With this conduct, the company was in gross violation of the aforementioned regulatory and statutory provisions. The Central Bank demanded that the company take remedial action, including revoking the amendments and informing Icelandic policyholders and distributors that it had done so. A transparency announcement about the case was published on the Central Bank website in June 2023. A notification that NBS had revoked NOVIS' operating licence was published that same month. Thereafter, the Central Bank published information for the company's customers on its website.

## Box 5

### Penalties

#### Cases concluded with sanctions in 2023

In 2023, the Central Bank concluded three cases involving violations by reaching a settlement with the parties concerned. One case was concluded with the levy of an administrative fine. Transparency announcements about these cases have been published on the Central Bank website. These four cases are described below.

#### Pension Fund for State Employees

In May 2023, the Central Bank and the Pension Fund for State Employees reached a settlement agreement providing for a fine in the amount of 2.5 m.kr. in a case involving the fund's violation of Article 58, Paragraph 1 of the Act on Insurance Activities, no. 100/2016, by failing to notify in advance its plans to acquire a direct qualifying holding in Vátryggingafélag Íslands hf. and an indirect qualifying holding in Líftryggingafélag Íslands hf.

#### Pension Fund for State Employees

In May 2023, the Central Bank and the Pension Fund for State Employees reached a settlement agreement provid-

ing for a fine in the amount of 2.5 m.kr. in a case involving the fund's violation of Article 58, Paragraph 1 of the Act on Insurance Activities, no. 100/2016, by failing to notify in advance its plans to acquire a direct qualifying holding in Vátryggingafélag Íslands hf. and an indirect qualifying holding in Líftryggingafélag Íslands hf.

#### Íslandsbanki hf.

In June 2023, the Central Bank and Íslandsbanki hf. reached a settlement agreement providing for a fine in the amount of 1.16 b.kr. in a case involving the bank's violation of further specified provisions of the Act on Markets in Financial Instruments, no. 115/2021, cf. Commission Delegated Regulation 2017/565, and the Act on Financial Undertakings, no. 161/2002, in its preparation and execution in connection with Icelandic State Financial Investments' 22 March 2022 offering of a State-owned 22.5% holding in Íslandsbanki hf., in that the bank failed to implement satisfactory governance and internal monitoring practices ensuring effective and prudent management,

failed to make audio recordings of telephone conversations, provided customers with incorrect information on the terms of offering, failed to comply with statutory requirements in its assessment of customers' applications for classification as professional investors; failed to take adequate measures to prevent conflicts of interests – e.g., in connection with employee and management participation in the offering – provided Icelandic State Financial Investments with misleading information on the classification of investors participating in the offering, failed to comply with Icelandic State Financial Investments' terms of offering, and was deemed to have failed, in its preparation and execution of the offering, to satisfy in all respects its obligation to operate honestly, fairly, and professionally in accordance with appropriate and sound business practices, with the credibility of the financial market and the interests of its customers as guiding principles.

#### Íslensk verðbréf hf.

In June 2023, the Central Bank and Íslensk verðbréf hf. reached an agreement to conclude by settlement, with payment of a fine in the amount of 2.6 m.kr., a case involving violations of Article 26 of Regulation (EU) no. 600/2014 on markets in financial instruments and amending Regulation (EU) no. 648/2012 (MiFIR); cf. Item 1 of Paragraph 1 of Article 3 of the Act on Markets in Financial Instruments, no. 115/2021; in that the company failed to notify the Central Bank of transactions it carried out with financial instruments during the period from September 2021 through December 2022.

#### Síminn hf.

In October 2023, the Financial Supervision Committee (FMEN) decided to impose an administrative fine in the amount of 76.5 m.kr. on Síminn hf. for the company's violation of then-current Article 122, Paragraph 1 of the Act on Securities Transactions, no. 108/2007, and Article 17(1) of Regulation (EU) no. 596/2014 on market abuse (MAR), by failing to publish, as soon as possible, insider information on the sale by Síminn hf. of Míla ehf. Síminn hf. has initiated legal action to demand the invalidation of the decision.

### Administrative fine cases brought before the courts in 2023

#### Fossar Markets hf. (now Fossar Investment Bank hf.)

In June 2020, the Central Bank decided to impose an administrative fine in the amount of 10.5 m.kr. on Fossar Markets hf. for violations of Article 57(a) of the Act on Financial Undertakings, no. 161/2002, and rules set on the

basis of that provision, in that the company paid bonuses to employees without having established a variable remuneration system. Fossar Markets hf. initiated legal proceedings against the Central Bank, demanding that the decision be invalidated and, in reserve, that the administrative fine be either cancelled or substantially reduced. With a judgment handed down by the District Court of Reykjavík on 12 October 2021 in Case no. E-6009/2020, the Court rejected the demand for invalidation of the Bank's decision. The company appealed the District Court judgment to the Court of Appeals. With a decision handed down on 17 February 2023 in Case no. 661/2021, the Court of Appeals upheld the District Court judgment.

#### Arion Bank hf.

In July 2020, the Central Bank decided to impose an administrative fine of 87,700,000 kr. on Arion Bank hf. for violations of then-current Article 122, Paragraph 1 of the Act on Securities Transactions, no. 108/2007. Arion Bank initiated legal proceedings against the Central Bank, demanding, as its primary claim, that the decision be invalidated, and as its reserve claim, that it be modified. With a judgment handed down by the District Court of Reykjavík on 19 April 2022 in Case no. E-6521/2020, the Central Bank's decision was upheld. The bank appealed the District Court judgment to the Court of Appeals. With a decision handed down on 9 June 2023 in Case no. 249/2022, the Court of Appeals upheld the District Court judgment.

#### Tryggingar og ráðgjöf ehf.

In November 2020, the Central Bank decided to impose an administrative fine in the amount of 35 m.kr. for violations by Tryggingar og ráðgjöf ehf. of Article 140(f), Paragraph 3 of the Act on Insurance Contracts, no. 30/2004, and Article 6, Paragraphs 1 and 2 of the same Act; cf. Article 32, Paragraph 1 of the Act on Distribution of Insurance, no. 62/2019. Tryggingar og ráðgjöf ehf. initiated legal proceedings against the Central Bank, demanding that the decision be invalidated and, in reserve, that the administrative fine be either cancelled or substantially reduced. With a judgment handed down by the District Court of Reykjavík on 9 March 2022 in Case no. E-506/2021, the Central Bank's decision to impose the administrative fine was upheld, but the amount of the fine was lowered to 33 m.kr. The company appealed the District Court judgment to the Court of Appeals, and the Central Bank filed a counterappeal. With a judgment handed down by the Court of Appeals on 29 September 2023 in Case no. 172/2022, the Central Bank's administrative decision concerning the violation of Article

6, Paragraphs 1 and 2 of Act no. 30/2004, cf. Article 32, Paragraph 1 of Act no. 62/2019, was upheld, while the decision pertaining to the violation of Article 140(f), Paragraph

of Act no. 30/2004 was invalidated. The fine was therefore reduced further, to 9 m.kr.

### **Information disclosures to customers of the Pension Fund of Commerce**

The Central Bank investigated the Pension Fund of Commerce's information disclosures made to fund members in advertisements and on its fund member website, in connection with changes made to members' pension rights. The aim of the investigation was to determine whether the pension fund had satisfied requirements that it provide correct and detailed information on its activities and services in advertisements and other promotional materials, as is provided for in the Act on Mandatory Insurance of Pension Rights and on Activities of Pension Funds, no. 129/1997. The Bank found the pension fund to be in violation of the requirements laid down in the Act. The Bank also demanded that changes be made to the information provided on the fund member website. On the same day that the Bank reached its conclusion in the case, a judgment was handed down by the District Court of Reykjavík in Case no. E-1722/2023, filed by a fund member against the pension fund. The Court found that the age-dependent reduction in pension rights via amendments to the Articles of Association, which took effect on 1 January 2023, was invalid, and the pension fund subsequently changed the information provided on its fund member website. The Supreme Court has accepted the pension fund's request to appeal the case to the court.

### **Investigation of dunning letters sent by collections agencies**

The Central Bank concluded an investigation of collection agencies' practices in connection with dunning letters. The aim of the investigation was to determine how the company satisfied the requirement that it send written collections notices pursuant to the Act on Collections, no. 95/2008. The Central Bank concluded that the wording of Article 7 of the Act on Collections does not exclude sending such notices by electronic means, and it therefore found no reason for further investigation of the matter.

The Central Bank's findings were based in part on the judgment handed down by the District Court of Reykjavík on 31 March 2023, in Case no. E-2483/2022,

in which the Court concluded that the aforementioned provision of the Act did not entail an obligation to send written collections notices solely by postal mail. The legal construction documents stated that the purpose of the bill of legislation preceding the Act on Collections was mainly to lay down certain fundamental principles on collections, for the benefit of consumers, and to reduce excess costs to debtors in connection with early-stage collections actions; i.e., with a Regulation placing limits on maximum collections costs. Sending collections notices to customers electronically, using an e-mail address provided by the borrowers themselves, must be viewed as promoting the aforementioned purpose of the law: to ensure that borrowers receive collections notices quickly and securely, and to reduce collections costs. The Court found therefore that sending mail electronically to an e-mail address expressly provided by the borrower to the lender for communications purposes satisfied the requirements of the Act on Collections, no. 95/2008, and it did not agree that Article 7 of that Act excluded such transmittals.

### **Other cases involving business conduct**

#### **Information on the revocation of NOVIS' operating licence**

In June 2023, the Central Bank published a press release stating that the National Bank of Slovakia (NBS) had revoked insurance company NOVIS' operating licence, effective 5 June 2023. NOVIS began operation in Slovakia in 2014 and sold products in Iceland, among other markets. With the withdrawal of its licence, NOVIS was prohibited to carry out insurance activities apart from those necessary to satisfy requirements and settle obligations. NBS is the competent supervisory authority in the company's home country.

The Central Bank has participated in a cooperative supervisory committee from EIOPA and has published further information on the NBS decision on its website, including what impact the revocation would have on Icelandic consumers, what measures were available to policyholders according to the terms of NOVIS contracts, and what points NOVIS policyholders should bear in mind. It was also reported that NBS had requested that

the Slovakian courts appoint a liquidator for NOVIS. As of this writing, no liquidator has yet been appointed. A liquidator's role would be to provide policyholders with further information on their rights, including the submittal of claims on the basis of insurance contracts, and to take a position on whether to request that the company be declared insolvent or whether its assets are sufficient to cover its obligations. The Bank is keeping abreast of developments and will update its information for Icelandic consumers accordingly.

#### **Circulars sent to consumer mortgage loan providers**

The Bank sent circulars to providers of consumer mortgages. The circulars highlighted providers' information disclosure obligations vis-à-vis consumers in connection with the Central Bank's Rules on Maximum Loan-to-Value Ratios for Mortgage Loans to Consumers, no. 702/2022 (now Rules no. 217/2024) and the Rules on Maximum Debt Service-to-Income Ratios for Mortgage Loans to Consumers, no. 701/2022 (now Rules no. 216/2024). The Bank pointed out the importance of ensuring that information provided in marketing materials and other information, such as on websites and in mortgage calculators, gives consumers legitimate expectations of whether or not they can take a loan, with reference to the aforementioned Rules. Because of this, lenders were instructed to review marketing materials, website information, and mortgage calculators aimed at consumers.

#### **Exemptions to securities licence requirements**

Two exemptions from securities licence requirements were granted in connection with employees of supervised entities. According to Article 40, Paragraph 3 of the Act on Markets in Financial Instruments, no. 115/2021, the Central Bank is authorised to grant a grace period of up to six months for new employees of an investment firm to acquire a securities licence and for employees who are required to hold a securities licence because of changes in their duties – e.g., as a result of promotion – if exceptional circumstances warrant such a grace period.

#### **Analysis of investment options for retail investors**

The Bank began analysing the investment options available to retail investors. It had previously conducted such an analysis twice. The newest analysis focuses on investment options available in 2021 and 2022. The Bank plans to publish its findings later this year in *Kalkofninn*, the Central Bank of Iceland's online publication portal for articles by staff members.

#### **Queries from consumers**

Each year, the Central Bank receives queries, comments, and complaints from the public concerning supervised entities' business conduct, and it provides information and guidance to the parties concerned. In 2023, the Bank received over 200 queries pertaining to business conduct and consumer affairs in the financial market. The Bank uses these queries to identify potential risks and failings, and in some instances such identification may cause the Bank to initiate a proactive investigation. The Central Bank does not issue rulings on disputes between financial market entities and their customers, however. On its website, the Central Bank publishes information on rulings committees and other options available to consumers in connection with their business with supervised entities, including entities licensed in other EEA countries.

### **Supervision of the securities market**

The Central Bank supervises the securities market in Iceland, in part to promote a market that is effective and secure. This supervision is carried out in a number of ways, such as ongoing supervision of information disclosures made by securities issuers, supervision of market participants' business conduct – including potential insider dealing and market abuse – and examination of data submitted to the Bank by supervised entities. Such data contain information on matters such as trading in equities, bonds, and derivatives; short positions; settlement failures; and so forth. In 2023, strong emphasis was placed on the quality of securities market entities' trade reporting system (TRS) filings, which provide key data for monitoring of market abuse. Furthermore, the Central Bank supervises the activities of the Nasdaq Iceland hf. securities exchange and two securities depositories. The Bank also cooperates with other Nordic financial supervisors in supervising the Nasdaq securities exchanges in the region. Furthermore, it is a member of a supervisory committee that includes representatives from competent authorities in the Baltic countries, with a focus on the activities of the Nasdaq CSD SE securities depository, whose activities extend to the entire Nordic-Baltic region. Among other tasks, the supervisory committee conducts an annual review and evaluation of the depository's operations.

#### **Supervision of market conduct, penalties, etc.**

In 2023, the Bank opened investigations of 33 cases stemming from the securities market, 16 of which resulted from tips submitted by Nasdaq Iceland. Most

## Outsourcing

New EBA Guidelines on outsourcing arrangements took effect within the EU in February 2019.<sup>1</sup> The Guidelines clarify the European supervisory bodies' priorities on outsourcing arrangements in the financial market and supervised entities' security vis-à-vis the risks that can arise if outsourcing is not handled adequately.

This extends to concerns about outsourcing of tech services, as network connections and cybersecurity were strained severely by the pandemic and the associated shift towards remote work, plus the war in Ukraine. Because of this, the European Systemic Risk Board (ESRB) issued a report focusing, among other things, on the value of establishing a coordination framework for cyber incidents.<sup>2</sup>

The Guidelines make tighter requirements for outsourcing arrangements, whether they involve domestic parties or the purchase of cloud services. They cover various aspects of outsourcing: policies, recording and documentation, preparation and risk assessments, and operation of outsourced activities.

The Guidelines entail a significant increase in supervision of outsourcing arrangements at companies within the EEA and stress, among other things, that risk manage-

ment and internal audit staff should review their processes for operational and management risk with an eye to the requirements laid down in the Guidelines.

In the past three years, supervised entities in Iceland have been subject to on-site and off-site inspections that either focus directly on outsourcing or include it in an examination of operational risk. Off-site inspections involving 25 entities are still ongoing. By now, most supervised entities are well aware of the outsourcing framework in effect for Iceland, although there is still room for improvement in many areas. These include clearer terms and conditions for outsourcing, regular updates of outsourcing policies and agreements, consideration of possible conflicts of interests in the contracting process, and a more formalised outsourcing structure under which the supervised entity is always responsible for outsourced projects.

It is clear that supervisory bodies in Europe are placing increased emphasis on supervised entities' outsourcing arrangements, and entities are encouraged to take appropriate measures to ensure that they adhere to the relevant Guidelines.<sup>3</sup>

1. See the circular distributed by the Financial Supervisory Authority to financial institutions, payment institutions, and electronic money institutions, no. 67/2019, announcing the entry into effect of the EBA Guidelines.
2. ESRB recommends establishing a systemic cyber incident coordination framework.

3. Guidelines on cloud-based outsourcing are in effect for markets supervised by EIOPA and ESMA: [Guidelines on outsourcing to cloud service providers](#) and [Guidelines On outsourcing to cloud service providers](#)

of these cases centred on issuers' information disclosure requirements and alleged market abuse. Of the cases investigated, 16 were concluded in 2023 and most of them were closed without a determination that a violation had been committed. In 2023, one case was concluded with the imposition of an administrative fine and another by settlement. Several other cases were concluded with a determination that a violation had been committed but without the imposition of penalties. The cases pertained, among other things, to the contents of prospectuses and to reporting due to securities trades and short positions.

In October 2023, the FMEN decided to impose an administrative fine in the amount of 76.5 m.kr. on

Síminn hf. In the decision, the Committee concluded that the company had violated then-current Article 122, Paragraph 1 of the Act on Securities Transactions, no. 108/2007, and Article 17(1) of Regulation (EU) no. 596/2014 (MAR) by failing to either publish insider information on the company's sale of Míla ehf. or postpone the publication of such information. The decision was published on the Central Bank website in November 2023.

In June 2023, Íslensk verðbréf hf. reached an agreement to settle a case involving the company's violation of Article 26 of Regulation (EU) no. 600/2014 (MiFIR) – cf. Article 3, Paragraph 1, Item 1 of the Act on Markets in Financial Instruments, no. 115/2021 –

by failing to notify the Central Bank of 6,126 trades in financial instruments that the company executed during the period between 1 September 2021 and 21 December 2022. Under the agreement, the company agreed to pay a fine in the amount of 2.6 m.kr. The settlement agreement was published on the Bank's website in August 2023.

### On-site inspections

As before, emphasis was placed on on-site inspections pertaining to financial undertakings' TRS II notifications of trades in financial instruments, with appraisals made of the internal organisational structure intended to ensure the quality of the notifications. Three such on-site inspections began in 2023 and were still ongoing at the year-end. One such on-site inspection carried out at Fossar Investment Bank hf. concluded in 2022, and a transparency announcement was published on the Central Bank website in July 2023.

In addition, the Central Bank completed an investigation of outsourcing arrangements at Nasdaq Iceland hf.

### Securities prospectuses

The Central Bank approved 23 prospectuses during the year, the same number as in 2022. The number of prospectuses has been broadly unchanged in recent years. As in 2022, two prospectuses were for public stock offerings, and admittance of the shares for trading on a regulated market were approved. The companies involved were Hampiðjan hf. and Ísfélag hf. Unlike the year before, the Bank approved two additional prospectuses in connection with the admittance of shares for trading on a regulated market when Amaroq Minerals Ltd. and Kaldalón hf. moved from the First North market to the Nasdaq Iceland Main Market.

Table I-1 Number of prospectuses and supplement approved by the Central Bank

|                   | 2021 | 2022 | 2023 |
|-------------------|------|------|------|
| Prospectuses      | 26   | 23   | 23   |
| Base prospectuses | 12   | 10   | 13   |
| Appendices        | 9    | 9    | 9    |

### Short positions in stocks

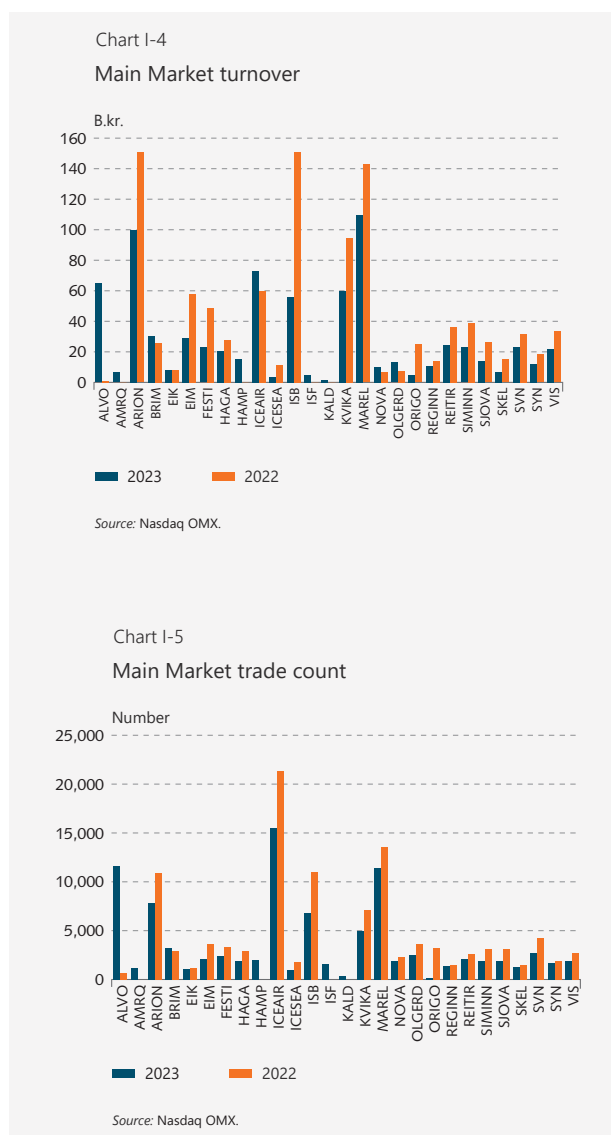
In spite of declines in the Nasdaq Iceland Main Market, there was a minor increase in the number of notifications of short positions. Table 2 gives a comparison of the number of notifications in 2022 and 2023, by month. In all, the Bank received 52 such notifications in 2023, as compared with 50 in 2022.

Table I-2 Notifications of short positions

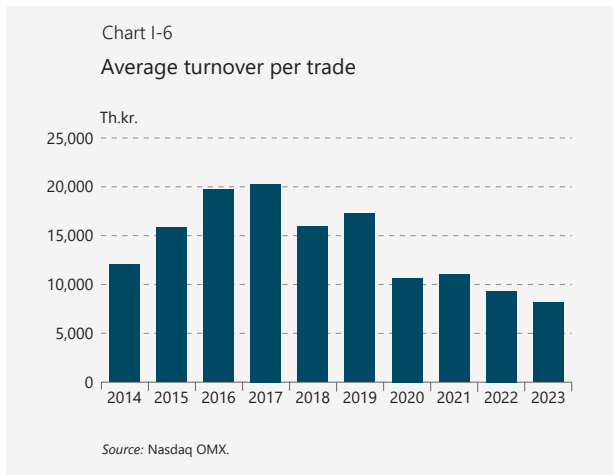
|           | 2022 | 2023 |
|-----------|------|------|
| January   | 2    | 5    |
| February  | 4    | 1    |
| March     | 6    | 7    |
| April     | 1    | 8    |
| May       | 3    | 2    |
| June      | 5    | 11   |
| July      | 2    | 2    |
| August    | 0    | 1    |
| September | 6    | 3    |
| October   | 16   | 2    |
| November  | 3    | 2    |
| December  | 2    | 8    |
| Total     | 50   | 52   |

### Developments in the securities market

Share prices fell marginally in 2023. The OMXI10 index fell by 1.7% and the OMXI index by 3.4%. Stock market prices fluctuated widely during the year, and in May







the OMX10 fell by 12.7%, its largest single-month drop since early 2009. It then rose by 16.2% over the last two months of the year. One new company was listed on the Main Market during the year – Ísfélag hf., which was admitted to trading in December. Three companies moved from First North to the Main Market: Amaroq Minerals Ltd, Hampiðjan hf., and Kaldalón hf. The exchange also approved the delisting of Origo hf. during the spring.

Turnover with shares of companies listed on the Main Market totalled just over 769 b.kr., a reduction of nearly 26% year-on-year. Turnover was strongest with shares in Marel hf. and Arion Bank hf., with trading in each of the two companies totalling around 100 b.kr. Chart I-4 shows the distribution of Main Market turnover, by company. The trade count was just over 94,000 in the Main Market, a contraction of 14.5% year-on-year. Trading was heaviest in Icelandair Group hf., with 15,531 trades, and in Marel hf., at 11,426 trades. Chart I-5 shows the distribution of trade counts in the Main Market, by company. The average amount per transaction was just over 8 m.kr., a decline of just under 13%. This average transaction amount was about half of the 2019 average. Chart I-6 shows developments in the average transaction amount from 2014 onwards. The average is much higher than in neighbouring countries, as can be seen in Table I-3.

Table I-3 Average turnover per trade<sup>1</sup>

|         |           |
|---------|-----------|
| Iceland | 8.158.055 |
| Denmark | 1.154.507 |
| Finland | 741.101   |
| Norway  | 606.447   |
| Sweden  | 577.877   |

1. Twelve-month daily average converted to ISK using month-end exchange rate.

Sources: Nasdaq OMX, Oslo Børs

## Supervision of funds and fund management companies

The Central Bank supervises both UCITS management companies, which are authorised to operate collective investment funds, and alternative investment fund managers, which are authorised to operate alternative investment funds for retail investors and other alternative investment funds. Such supervision centres mainly on whether or not the funds in question invest in accordance with statutory authorisations and their own internal rules. Factors such as risk management, conflicts of interests, and liquidity management are monitored as well, as are the obligations of fund custodians.

At the end of 2023, six fund management companies were operating in Iceland, all of which had also received licences to manage alternative investment funds. In addition, six companies were licensed only as alternative investment fund managers. Three of these licences were granted in 2023. An additional 18 companies were registered as alternative investment fund managers, including one securities firm. Six new management companies were registered in 2023.

At the end of the year, 38 UCITS funds, 76 alternative investment funds for retail investors, and 131 other alternative investment funds were supervised by the Central Bank. A total of seven new alternative funds for retail investors and 13 other alternative investment funds were established in 2023, while the number of UCITS funds remained unchanged during the year.

### Applications for marketing authorisation

The Central Bank authorised eight domestic alternative investment funds to market their products and services to professional investors in Iceland in 2023. Furthermore, the Central Bank received a large number of applications from third-country (i.e., non-EEA) management companies and alternative investment funds seeking authorisation to market products to professional investors in Iceland. Applications from 13 management companies and 20 alternative investment funds were approved during the year. At the end of 2023, 44 fund managers and 94 alternative investment funds from third countries were authorised to market products to professional investors in Iceland.

### Improvements and reforms

During the year, the Bank emphasised internal improvements entailing the completion of work on the design of data testing in order to ensure improved data quality. For instance, the Bank completed its work on the

## IT risk – Central Bank priorities and the steps ahead

Risk associated with use of information and communications technology (ICT) is and will remain a point of focus for the Central Bank. It is important that supervised entities make an effort to ensure that risks are known, assessed, and mitigated to the extent possible, so that the security of data and services is assured. The Bank's supervision is risk-oriented, and its scope is determined in part by the size of the entity, its importance for the financial market, and the risks that, in the Bank's opinion, could be faced by the undertakings and its customers.

In 2019, prior to its merger with the Central Bank, the Financial Supervisory Authority issued the Guidelines on Risk in the Operation of Supervised Entities' Information Systems, no. 1/2019, which set forth harmonised criteria for the operation of information technology risk management systems and outlined the controls that supervised entities should have in place in order to manage that risk. Since then, EBA and EIOPA have issued European Guidelines on information and communications technology (ICT) and security risk management, which have to some extent replaced the Icelandic Guidelines.

As large and serious incidents relating to tech services become more common in the financial market, international discussion and concerns about ICT risk gain prominence, not least within the EU. As a result, the EU has issued a Regulation for the financial market entitled the Digital Operational Resilience Act (DORA). DORA will take effect within the EU at the beginning of 2025. The incorporation of the Regulation into the EEA Agreement and Icelandic law is currently underway.

DORA is broad in scope, and the Central Bank encourages all financial undertakings to acquaint themselves with it, as its implementation will affect the entire financial market. Nevertheless, DORA observes the principle of proportionality, in that it makes less stringent requirements of smaller supervised entities. A detailed discussion of its contents is beyond the scope of this report, but key points

relating to its impact on the Icelandic financial market can be found below.

The Regulation implements provisions requiring management of ICT risk. DORA emphasises that financial market entities should have in place a sound management structure for information security, with the involvement and oversight of the board of directors, and that they should have well defined areas of responsibility, with separation between them. It is also required that entities have in place an ICT policy ICT rules, and procedures for change management and monitoring of ICT risk. Financial market entities are required to maintain a list of business processes, ICT systems, data, and connections between them, classified by level of importance.

There are requirements for registration and notification of operational incidents, as well as responses to them. There are also requirements concerning emergency plans and business continuity plans. An emergency plan is the plan that financial undertakings' ICT employees follow during resolution of serious incidents such as an interruption in internet connections. On the other hand, a business continuity plan is the plan that senior management follows in order to keep operations up and running while the incident is being resolved. Among other requirements, entities must conduct regular tests of these plans and must carry out risk-based tests of resilience against cyberattacks, called threat-led penetration testing (TLPT).

Under DORA, more stringent requirements are made of supervised entities that make use of third-party services. Larger service providers that are designated as important to the internal market will be included in the so-called Union Oversight Framework according to DORA.

Below are some of the main provisions included in DORA. The Central Bank has been preparing for the incorporation of DORA into Icelandic law and encourages entities to begin considering the changes they must make in order to satisfy the requirements therein.

design of data testing of filings submitted by alternative investment funds via the Bank's data submission system. Furthermore, the Bank developed a tool for automated analysis of data submitted on a regular basis by funds and fund managers. Moreover, foreign

entities were granted access to the Bank's data submission system using two-factor authentication, which made it possible to receive their filings through the system instead of via e-mail.

## Supervision of anti-money laundering and terrorist financing measures

The Central Bank carries out risk-based supervision of entities subject to notification requirements (obliged entities) in accordance with the Act on Measures Against Money Laundering and Terrorist Financing, no. 140/2018. Risk-based supervision is a methodology that entails assessing the risk of money laundering and terrorist financing in the financial market and prioritising supervisory measures in accordance with the results of that assessment. It implies, among other things, that supervision is more frequent and more thorough where the risk is deemed to be greatest.

There were 105 such obliged entities at the end of 2023, up from 97 a year earlier. They include financial undertakings, payment institutions, electronic money institutions, UCITS management companies, alternative investment fund management companies, life insurance companies, pension funds, currency exchange services, and virtual currency service providers, as well as branches, agents, and distributors representing foreign financial institutions in Iceland.

### On-site and off-site inspections

Inspections on obliged entities' AML measures may take the form of on-site inspections or off-site inspections. They may be theme-based inspections in which the same factors are examined at numerous obliged entities. The Bank carried out a number of inspections in 2023. It conducted on-site inspections and other follow-up inspections focusing on risk assessments, risk-based measures taken by supervised entities, and other matters.

In addition to the above, the Bank uses other methods to highlight obliged entities' obligations or to gather information on measures carried out by them. Examples of such methods include presentations given by the Bank, as well as guidance given in response to queries received from obliged entities. Furthermore, during the year the Bank worked towards strengthening cooperation and exchange of information between supervision of AML measures, on the one hand, and prudential supervision of the same measures on the basis of the EBA Guidelines, on the other.

### On-site inspections

On-site inspections were carried out at Arion Bank hf., Íslandsbanki hf., and Kvika banki hf., with the aim of examining on the entry and traceability of data in

the banks' systems, as well as examining items relating to the previous on-site inspection of their risk assessments and risk-based measures. The inspections extended only to certain risk factors in the banks' risk assessment. The Central Bank also examined how the banks carried out customer risk classification, customer due diligence, and on-going monitoring with reference to the risk assessment. A comparable investigation at Landsbankinn hf. concluded in 2022, and the results were published in a transparency announcement posted on the Central Bank website in December 2023.

An on-site inspection was also conducted at Sparisjóður Höfðhverfinga ses., with the aim of evaluating the savings bank's internal risk assessments, as well as its policies, controls, and procedures for reducing the risk of money laundering and terrorist financing. In that inspection, the Central Bank also examined factors including how the bank carried out customer risk classification, customer due diligence, and on-going monitoring with reference to the risk assessment. The Bank also examined points relating to international sanctions and compliance with the then-current Act on the Freezing of Funds and Designation of Entities on Sanctions Lists in Relation to Terrorism Financing and Proliferation of Weapons of Mass Destruction, no. 64/2019 (now Act no. 68/2023). Finally, the Bank examined how the savings bank approached training and educational efforts, how money laundering reporting officer carried out his duties, and how the bank fulfilled its obligation to investigate and reporting.

### Off-site inspections

In 2023, the Bank investigated compliance with the Act on Measures against Money Laundering and Terrorist Financing by carrying out inspections at ALM Verðbréf hf.; fund management companies and alternative investment fund managers Akta sjóðir hf., Íslandssjóðir hf., ÍV sjóðir hf., Landsbréf hf., Stefnir hf. and Summa Rekstrarfélag hf.; registered alternative investment fund managers Alfa Framtak ehf., Algildi GP ehf., Crowberry Capital GP ehf., Eyrir Venture Management ehf., Frumtak Ventures ehf., Ísafold Capital Partners ehf., Óðinn Capital ehf., Spakur Finance sf., and Vex ehf.; as well as Greiðslumiðlun ehf. and Síminn Pay ehf., which are registered as consumer loan providers. The inspections entailed an examination of their business-wide risk assessments. The results of the inspections were published in a transparency announcement on the Central Bank website in July 2023.

## Appraisals

### FSAP

As is noted above, the IMF completed its Financial Sector Assessment Program (FSAP) appraisal of the Icelandic financial system during the year. The appraisal included supervision of AML measures. Following the appraisal, the Fund recommended improvements to the Central Bank's risk assessments of obliged entities and its supervision of banks and virtual currency service providers.

### Regional appraisal of AML measures

In September 2023, the IMF published its Regional Nordic-Baltic Technical Assistance Report on Financial Flows Analysis, AML/CFT Supervision and Financial Stability. The report was issued pursuant to technical assistance provided by the IMF to the authorities in the Nordic and Baltic countries with the aim of enhancing the efficacy of their national and regional anti-money laundering and terrorist financing frameworks. The report notes that continuous efforts to strengthen AML/CFT frameworks is a clear priority in the region and that coordinated action and innovative solutions are key in keeping pace with evolving financial integrity risks.

The Central Bank considers the analysis and outcome of the regional assessment project useful and hopes that, with the publication of the report, the private sector and other countries take key learnings from experience and good practice in the region. The Central Bank works continuously on further improving its supervision of measures against money laundering and terrorist financing, and its action plan is in line with the recommendations in the IMF report. This includes further development of risk assessments and risk-based supervision, use of information on financial flows in the risk assessment process, and further analysis of information on cross-border financial flows. Nordic-Baltic experts in financial stability and AML measures will collaborate on the implementation of the IMF's recommendations in order to strengthen the Nordic-Baltic countries in their efforts to combat money laundering and terrorist financing in the financial sector.

## Educational material and guidelines

### Educational material on the risks attached to virtual assets

In August 2023, the Central Bank issued educational material on risks associated with virtual assets. The aim of this material is to provide guidance to obliged entities that offer virtual currency services. It is also

intended to make it easier for entities in this market to identify risks pertaining to money laundering and terrorist financing and to provide guidance on business-wide and individual risk assessments.

### Informational meeting for consumer loan providers

In September 2023, the Central Bank held an informational meeting for loan providers pursuant to the Act on Consumer Credit, no. 33/2013, which fall under the Bank's supervision pursuant to the Act on Measures against Money Laundering and Terrorist Financing. The aim of the meeting was to provide information to the loan providers in question about their main obligations under the law and the risks they must bear in mind in connection with their AML measures.

### Updated lists of politically exposed occupations and high-risk jurisdictions

In 2023, the Bank issued an updated list of occupations classified as high-level public positions in connection with its assessment of politically exposed persons. The update was prepared in March 2023. Furthermore, as it has done in the past, the Bank updated its list of high-risk and uncooperative jurisdictions three times during the year, in accordance with changes made to comparable lists issued by the Financial Action Task Force (FATF) and the EU.

### Adoption of EBA Guidelines

The Central Bank adopted the EBA Guidelines on the use of remote customer onboarding solutions. The Bank also adopted amendments to the EBA's ML/TF Risk Factors Guidelines, on the one hand, and the EBA Guidelines on policies and controls for the effective management of ML/TF risks when providing access to financial services.

### Conference

In November 2023, the Central Bank held a conference on measures against money laundering and terrorist financing, bringing together Icelandic and foreign experts in the field. The conference covered a range of issues, including the state of affairs in Iceland, risk-based supervision, and cooperative efforts to combat money laundering and terrorist financing.

# Key priorities in the 2024 work timetable



## Priorities for 2024

The Central Bank prepares a detailed supervisory timetable each year. This work is based in part on the Bank's Supervisory Strategy for 2022-2024, which is still in effect. It is also based on recent risk assessments and the current strategic supervisory priorities prepared by EBA, EIOPA, and ESMA. The Central Bank publishes the key priorities in its supervisory timetable in order to inform supervised entities of its priorities for the coming year, thereby enabling them to give consideration to these priorities in their operations.

### Emphasis on risks relating to high interest rates and inflation

The external economic environment has changed radically in recent years, but the domestic financial market has retained its strength in the face of these changes. The fall of Silicon Valley Bank in the US in March 2023 and the takeover that prevented the fall of Credit Suisse, with the subsequent involvement of the Swiss authorities, caused tremors in international markets. These events directed supervisory bodies' attention to the impact of rising interest rates on the financial system and highlighted the importance of creating a strong framework that would enable banks to handle operational headwinds.

As a result, this year's supervisory timetable provides for appraisals of key risks relating to high interest rates and inflation, especially credit risk and large exposures, including how supervised entities connect large borrowers. In addition, given the economic environment, the timetable provides for assessing pension funds' credit risk frameworks and monitoring, as well as

their frameworks for real estate-backed loans to fund members.

### Emphasis on ICT risk and the operational resilience of the financial system

Although the financial system has shown its strength in recent years, significant challenges and risks still lie ahead, and supervised entities must respond by taking action so as to bolster the operational resilience of the financial system.

Western countries imposed economic sanctions on Russia in response to its invasion of Ukraine, and there was reason to fear that Russia would retaliate by mounting cyberattacks on the countries concerned. These circumstances highlighted how important it is that Icelandic supervised entities have in place a robust cybersecurity system to guard against such attacks. As a result, the financial market has had to respond to elevated cyber- and IT risk, and market participants must continue to make adaptations aimed at ensuring adequate preparedness and meeting the growing requirements made of the market in this area. Cyber- and IT risk, or ICT risk, is currently prioritised by European financial supervisory bodies, as well as by the Central Bank. The goal is to strengthen the resilience and defences of supervised entities facing broad-based digital transformation and the associated increase in risk, which simultaneously includes the growing threat of cyberattacks and fraud and extends to market abuse, money laundering, and a range of other weaknesses that must be addressed with targeted measures.

The Central Bank's supervisory timetable for 2024 includes inspections and checks aimed at contingency and business continuity frameworks, as well as spe-

cific aspects of IT systems relating to acquiring. The Bank also plans to conduct checks on oversight and structure of procedures, and on supervised entities' operational risk.

Further ahead, there are plans to pass legislative amendments so as to tighten the ICT security requirements made of supervised entities. This amending legislation will incorporate the Regulation (EU) 2022/2554 on digital operational resilience for the financial sector (DORA) into Icelandic law. Among other things, the Regulation lays down harmonised requirements pertaining to the security of ICT systems, management of risk associated with digital services, reporting in connection with such risk, and testing and risk assessment in connection with outsourcing ICT services to a third party. It is important that supervised entities prepare for the changes that the legislation will bring.

### **Focus on business conduct and governance practices**

In 2023, an investigation by the Central Bank revealed flaws in governance and internal controls at a systematically important bank in connection with the sale of a holding in the bank itself. The Bank's findings in that case underscore the urgent need for financial market participants to examine their governance practices and company culture so that they can ensure that they operate in accordance with sound and appropriate business practices. The case also highlights the need for securities market participants to operate with integrity and professionalism, thereby promoting investors' confidence in the market. Among the weaknesses revealed by the investigation were failures in record-keeping and storage of data, including audio recordings of telephone conversations, and in classification of customers.

Investigating how these matters are handled by supervised entities and demanding remedial action where necessary is a priority issue. The Bank will focus on determining whether supervised entities in the securities market satisfy requirements on recordings of telephone calls and other digital communications with customers. Furthermore, supervisory action will cover, among other things, the classification of customers in accordance with the Act on Markets in Financial Instruments, no. 115/2021.

The rights of supervised entities' customers – including the handling of complaints and the disclosure of information on costs and fees – will continue to be of core importance to the Central Bank. Moreover, the implementation of supervised entities' obligations

under the Act on Payment Accounts, no. 5/2023, will be enforced.

This year's supervisory timetable also prioritises checks on supervised credit institutions' risk management frameworks and conduct risk, as well as consolidated entities' governance practices.

In the insurance market, the Bank will continue to place emphasis on investigations relating to governance practices and tasks focusing on actuaries. Conduct risk and business practices in the insurance market will also be prioritised.

In the pension market, the Bank will continue to monitor board members' risk awareness, risk culture, and analysis of conflicts of interests, as well as pension funds' internal controls. In addition, the Bank monitors practices and frameworks for pension funds' actuarial assessments.

### **Focus on sustainable finance**

Within the EEA, increasing attention is directed at ensuring that the financial market assesses and manages its climate risk, including transition risk, and that it contributes to the achievement of climate targets.

In mid-2023, new legislation implementing two EU sustainability regulations entered into force in Iceland: the SFDR-Regulation and the Taxonomy Regulation. In 2024, supervised entities will be asked to make an assessment of implementation and compliance with the new framework.

### **Focus on anti-money laundering and terrorist financing measures**

Supervision of measures to combat money laundering and terrorist financing in the financial market has been systematically increased in recent years. In 2023, the Central Bank made comments and recommendations on several supervised entities' anti-money laundering and terrorist financing measures. Although significant progress has been made in this area in recent years, there is still a need for a variety of reforms in the Icelandic financial market, as the Central Bank's supervisory priorities for 2024 show clearly.

The Bank's supervisory timetable for 2024 continues to emphasise strongly that obliged entities should strengthen their defences against money laundering and terrorist financing. The Bank's inspections will focus, among other things, on obliged entities' business-wide and individual risk assessments; the tech solutions they use for ongoing supervision; the extent to which their policies, controls, and procedures satisfy statutory requirements; and their fulfilment of the obli-

gation to investigate and notify. In assessing the suitability and qualifications of obliged entities' executives, the Bank will continue to emphasise their knowledge in this area. The Bank will also stress matters centring on access to financial services and management of risk, or de-risking, as well as supervision of entities on sanctions lists.

### **Emphasis on data quality**

Data from supervised entities are an important part of the Central Bank's supervisory work, and stronger emphasis has been placed on verifying data quality in recent years. Among other things, the Bank has prioritised trade reporting system (TRS) data and supervised entities' TRS-related filings, which are used for ongoing monitoring of market transactions. The 2024 supervisory timetable will continue to prioritise data quality, which the Bank plans to follow up with checks and investigations, including ongoing monitoring to review and verify the quality of supervised entities' TRS-related data and filings, as well as checks on the quality of credit registry data concerning links between parties and classification of loans. Emphasis will also be placed on following up on the implementation of new reporting requirements and the quality of filings submitted by alternative investment fund managers.

# Amendments to regulatory instruments in the financial market



This section gives an overview of financial market legislation passed in Iceland in 2023, followed by a list of other regulatory instruments pertaining to the financial market and either set or adopted during the year. Thereafter is an overview of forthcoming financial market legislation.

## Statutory amendments in 2023

The Central Bank of Iceland participates actively in shaping the regulatory framework for the financial market in Iceland, including by setting rules and adopting guidelines from the following European financial market supervisors; i.e., the European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA), and European Securities and Markets Authority (ESMA).<sup>1</sup> Furthermore, Bank staff participate in ministerial committees and task forces entrusted with preparing bills of legislation that apply to the activities of supervised entities. The Bank plays a key role in the financial market in terms of monitoring, adopting, and implementing technical standards, guidelines, and recommendations issued by European financial market supervisors. The Central Bank oversees regulatory authorisations applying to the Icelandic financial market, enforces and interprets the relevant regulatory instruments, and keeps abreast of forthcoming EEA-wide amendments, and considers these activities an important part of its role.

The following acts of law pertaining to the financial market were passed by Parliament in 2023:

- Act on Implementation of International Sanctions and Freezing of Funds, no. 68/2023.

1. Also included in the group of European financial market supervisors is the European Systemic Risk Board (ESRB).

- Act no. 64/2023 amending the Act on Alternative Investment Fund Management Companies, the Act on UCITS and Investment Funds, and other acts of law (cross-border sale of funds, master funds, and feeder funds, etc.).
- Act no. 63/2023 amending the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020 (minimum required own funds and eligible liabilities, etc.).
- Act no 49/2023 amending the Act on the Central Bank of Iceland, no. 92/2019 (Financial Supervision Committee).
- Act on Securities Financing Transactions, no. 41/2023.
- Act on Sustainability-Related Disclosures in the Financial Services Sector and a Taxonomy for Sustainable Investments, no. 25/2023.
- Act no. 12/2023 amending the Act on Mandatory Insurance of Pension Rights and on Activities of Pension Funds, no. 129/1997 (foreign exchange risk and information disclosure to fund members).
- Act no. 10/2023 amending the Act on Financial Undertakings and the Act on Insurance Activities (residency requirements for managing directors and board members).
- Act no. 7/2023 amending the Act on Covered Bonds and the Act on Financial Undertakings (covered bonds).
- Act on Money Market Funds, no. 6/2023.
- Act on Payment Accounts, no. 5/2023

## Rules, Icelandic and European guidelines, and benchmarks issued in 2023

### Rules

In 2023, the Central Bank of Iceland set the following rules pertaining to the financial market for the purpose



of, among other things, incorporating EU regulations on technical standards adopted by European financial market supervisors into Icelandic law:

- Rules on Financial Undertakings' Market Risk, no. 1681/2023.
- Rules on Financial Undertakings' Credit Risk, no. 1680/2023.
- Rules on Securities Financing Transactions, no. 1560/2023.
- Rules on Harmonised Assumptions Underlying the Standardised Rule for Calculating the Solvency Capital Requirement, no. 1441/2023.
- Rules on Technical Information for the Calculation of Technical Provisions and Basic Own Funds for Reporting with Reference Dates from 31 March 2023 through 29 September 2023, no. 1440/2023.
- Rules on Strong Customer Authentication and Common and Secure Open Standards of Communication in Payment Services, no. 1360/2023.
- Rules on Derivatives Trading, Centralised Counterparties, and Trade Repositories, no. 1300/2023.
- Rules on Central Bank of Iceland Information Disclosures Relating to Cross-Border Distribution of Collective Investment Undertakings, no. 1126/2023.
- Rules on Financial Undertakings' Credit Risk, no. 1092/2023 (abrogated upon the entry into effect of Rules no. 1680/2023 on the same topic).
- Rules on the Mapping of Credit Assessments in Calculation of Own Funds Requirements for Credit Risk and Securitisation, no. 1091/2023.
- Rules on Supervision of the Use of the Internal Ratings-Based Approach to the Calculation of Financial Undertakings' Own Funds Requirements, no. 1090/2023.
- Rules on Securities Settlement and Central Securities Depositories, no. 1055/2023.
- Rules on Transparency Requirements in Markets in Financial Instruments, no. 983/2023.
- Rules on Operating Licences and Organisational Requirements of Investment Firms, Provision of Information in Connection with Qualifying Holdings, and Criteria for Ancillary Activities, no. 982/2023.
- Rules on Derivatives and Clearing for Financial Instruments, no. 981/2023.
- Rules on Financial Undertakings' Information Disclosure Requirements, no. 772/2023.
- Rules on Information Disclosure Relating to Applications for Licensing as a Credit Institution, no. 771/2023.
- Rules on Financial Undertakings' Market Risk, no. 751/2023 (abrogated upon the entry into effect of Rules no. 1681/2023 on the same topic).
- Rules on Financial Undertakings' Credit Risk, no. 750/2023 (abrogated upon the entry into effect of Rules no. 1092/2023 on the same topic).
- Rules on Securities Issuers' Information Disclosure Requirements, no. 655/2023. Rules on Reporting Requirements for Money Market Fund Managers, no. 587/2023.
- Rules on Definitions and Criteria for European Long-Term Investment Funds, no. 586/2023.
- Rules on Maximum Loan-to-Value Ratios for Mortgage Loans to Consumers, no. 550/2023 (abrogated upon the entry into effect of Rules no. 217/2024 on the same topic).
- Rules on the Framework for Transactions with Financial Instruments, no. 545/2023.
- Rules on the Preparation and Provision of Key Information Documents for Retail Investors, no. 510/2023.
- Rules on Standardised Terminology and Standardised Presentation of Price Lists and Fee Summaries for Payment Services, no. 485/2023.
- Rules on Transmission of Information Relating to Resolution of Credit Institutions and Investment Firms, no. 398/2023.
- Rules on Supervision of the Use of the Internal Ratings-Based Approach to the Calculation of Financial Undertakings' Own Funds Requirements, no. 397/2023 (abrogated with the entry into effect of Rules no. 1090/2023 on the same topic).
- Rules on Calculation of Financial Undertakings' Large Exposures, no. 396/2023.
- Rules on the Appointment of Central Contact Points for Payment Services, no. 395/2023.
- Rules on Technical Information for the Calculation of Technical Provisions and Basic Own Funds for Reporting with Reference Dates from 31 December 2022 through 30 March 2023, no. 388/2023.
- Rules on Countercyclical Capital Buffers for Financial Undertakings, no. 256/2023.
- Rules on Price Indexation of Savings and Loans, no. 218/2023.
- Rules on Covered Bonds, no. 190/2023.
- Fee schedule for Tasks Relating to Financial Supervision, no. 165/2023.
- Rules on Suitability Assessments for Managing Directors and Board Members of Currency Exchange Service Providers and Virtual Currency Service Providers, no. 152/2023.

- Rules on Registration of Currency Exchange Service Providers and Virtual Currency Service Providers, no. 151/2023.
- Rules on Technical Information for the Calculation of Technical Provisions and Basic Own Funds for Reporting with Reference Dates from 30 September 2022 through 30 December 2022, no. 140/2023 .
- Fee schedule for Tasks Relating to Financial Supervision, no. 130/2023 (abrogated with the entry into effect of Fee schedule no. 165/2023 on the same topic).
- Rules on Securities Settlement and Central Securities Depositories, no. 80/2023 (abrogated with the entry into effect of Rules no. 1055/2023 on the same topic).
- Rules on the Role and Position of Compliance Officers and the Documentation of Communications under the Act on Measures to Combat Market Abuse, no 44/2023

#### Icelandic guidelines

The Central Bank did not issue any new Icelandic guidelines during the year.

#### European guidelines

The European financial market supervisory bodies issue guidelines pursuant to the authorisation in Article 16 of the Regulations Establishing a European Supervisory Authority, no. 1093-1095/2010, which were incorporated into Icelandic law with the Act on a European Financial Supervisory System, no. 24/2017. The purpose of such guidelines is to bring about harmonised, successful, and effective supervisory execution within the European financial supervisory system and to ensure collective, homogeneous, and harmonised application of EU legislation.

When European guidelines pertaining to market entities are adopted by the Central Bank, an explanatory circular is sent to these entities, together with a link to the English version. The documents are also published on the Central Bank website. After European guidelines have been adopted by the Central Bank, the Bank uses them as a basis for its supervisory activities.

During the year, the Central Bank adopted the following European guidelines:

- Guidelines on methodology, oversight function, and record keeping under the EU Benchmarks Regulation (ESMA81-393-288).
- Guidelines on non-significant benchmarks under the Benchmarks Regulation (ESMA70-145-1209).
- Guidelines on central securities depositories' access to trading feeds of central counterparties and trad-

- ing venues in accordance with Article 53(3) of Regulation (EU) no. 909/2014 on improving securities settlement in the European Union and on central securities depositories (ESMA70-151-298).
- Guidelines on the management body of market operators and data reporting services providers (ESMA70-154-271).
- Guidelines on the process for the calculation of the indicators to determine the most relevant currencies in which settlement takes place under Article 12(1) (b) of the Central Securities Depositories Regulation (ESMA70-708036281-66).
- Guidelines on the process for the calculation of the indicators to determine the substantial importance of a central securities depository for a host member state under Article 24 of the Central Securities Depositories Regulation (ESMA70-708036281-67).
- Guidelines on the reporting to competent authorities under Article 37 of the Money Market Fund Regulation (ESMA34-49-173).
- Guidelines on stress test scenarios under the Money Market Regulation (ESMA34-49-446).
- Guidelines on the application of C6 and C7 of Annex 1 of MiFID II (ESMA-70-156-869).
- Guidelines on disclosure of non-performing and forbore exposures (EBA/GL/2022/13).
- Guidelines on overall recovery capacity in recovery planning (EBA/GL/2023/06).
- Guidelines on improving resolvability for institutions and resolution authorities under Articles 15 and 16 of Directive 2014/59/EU (*Resolvability Guidelines*) (EBA/GL/2022/01).
- Guidelines on the conditions to be met to benefit from an exemption from contingency measures under Article 33(6) of Regulation (EU) 2018/389 on strong customer authentication and secure communication (EBA/GL/2018/07).
- Guidelines amending the ML/TF Risk Factors Guidelines (EBA/GL/2023/03).
- Guidelines amending Guidelines EBA/GL/2022/01 on improving resolvability for institutions and resolution authorities under Articles 15 and 16 of Directive 2014/59/EU (*Resolvability Guidelines*), to introduce a new section on resolvability testing (EBA/GL/2023/05).
- Guidelines on the use of remote customer onboarding solutions (EBA/GL/2022/15).
- Guidelines on management of interest rate risk and credit spread risk arising from non-trading book activities (interest rate risk in the banking book

(IRRBB) and credit spread risk in the banking book (CSRBB)) (EBA/GL/2022/14).

- Guidelines on policies and controls for the effective management of ML/TF risks when providing access to financial services (EBA/GL/2023/04)

### Benchmarks

The Bank adopted one set of benchmarks during the year: *Common procedures and methodologies for the supervisory review and evaluation process (SREP Guidance)* (no. 1/2023). This is a revision based on the EBA Guidelines on the same topic, which took effect in January 2023 (EBA/GL/2022/03). The aim of the benchmarks is to articulate methodologies and execution of the SREP assessments carried out by the Central Bank on financial undertakings. The Bank began revising the aforementioned benchmarks during the year and reissued them in January 2024.

### Forthcoming new financial market legislation

This section gives an overview of financial market legislation set for passage in 2024. Central Bank experts participate in this work in various ways, such as cooperating with Government ministries in drafting bills of legislation and regulations, participating in issuing rules and guidelines, and adopting European guidelines.

### Regulation on distributed ledger technology (DLT)

Regulation (EU) 2022/858 on a pilot regime for market infrastructures based on distributed ledger technology establishes an experimental framework for DLT-based infrastructure; i.e. a multilateral trading facility, a settlement system, and systems functioning as both trading and settlement systems. The term *DLT financial instrument* is defined, and requirements laid down in current directives and regulations (MiFID II, MiFIR, and CSDR) are adapted to the unique challenges entailed in technological advances. One of the aims of the Regulation is to fill gaps in the existing European regulatory framework. A bill of legislation incorporating the Regulation into Icelandic law is set for introduction at the spring 2024 legislative session.

### Bill of legislation amending the Act on Mandatory Insurance of Pension Rights and on Activities of Pension Funds, no. 129/1997 (investment authorisations and supplemental pension savings)

It is planned to introduce a bill of legislation amending Act no. 129/1997 at the spring 2024 legislative session. The aim of the bill is to increase individuals' freedom of

choice in investing voluntary supplemental pension savings. The bill includes provisions stipulating that individuals themselves should be able to select the investment strategy applying to such savings and that they should be authorised to make changes to their investment strategy in consultation with the pension custodian.

### Directive and Regulation on prudential supervision of investment firms (IFD and IFR)

Directive (EU) 2019/2034 and Regulation (EU) 2019/2033 on prudential supervision of investment firms (IFD and IFR) set forth harmonised requirements for prudential supervision of investment firms falling within the scope of MiFID II. They specify the required minimum level of initial capital for investment firms, the powers and tools that supervisory authorities must have in order to supervise investment firms, and the information that supervisory authorities must publish. A bill of legislation incorporating these instruments into Icelandic law is set for introduction at the autumn 2024 legislative session.

### Review of regulations establishing EBA, EIOPA, ESMA, and ESRB (European supervisory authorities review)

Regulation (EU) 2019/2175 contains amendments to Regulations (EU) no. 1093-1095/2010 establishing the European financial market supervisory authorities EBA, EIOPA, and ESMA. Changes were made to the organisational structure of the institutions; furthermore, ESMA was entrusted with direct supervision of EU critical benchmarks and their administrators and data service providers, in accordance with the MiFID II/MiFIR framework. For EEA-EFTA states, supervision will be in the hands of the EFTA Surveillance Authority (ESA). Amendments were also made to foster supervisory convergence and improved investor protection. Regulation (EU) 2019/2176 made various amendments to Regulation (EU) no. 1092/2010, which established the European Systemic Risk Board (ESRB). It is particularly noteworthy that amendments are made concerning participation by non-EU countries in the ESRB's activities, when opens the possibility for EEA-EFTA states to become full non-voting members, an option they already have for EBA, EIOPA, and ESMA. A bill of legislation incorporating the Regulation into Icelandic law is set for introduction at the autumn 2024 legislative session.

### Transfer of supervision of data reporting services providers

Directive (EU) 2019/2177 on the transfer of supervision of data reporting service providers contains amendments to MiFID II (Directive 2014/65/EU), Solvency II

(Directive 2009/138/EC), and the Money Laundering Directive (Directive (EU) 2015/849); furthermore, it transfers supervision of data reporting services providers to ESMA. For EEA-EFTA states, supervision will be in the hands of the EFTA Surveillance Authority (ESA). A bill of legislation incorporating the Directive into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### OTC derivatives, central counterparties, and trade repositories (EMIR 2.2. CCP)

Regulation (EU) 2019/2099 is part of the review of the regulatory framework for derivatives. It amends Regulation (EU) no 648/2012 (EMIR) with the aim of strengthening supervision of central counterparties (CCP). A bill of legislation incorporating the Regulation into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### Regulation on a framework for simple, transparent, and standardised securitisation (STS)

Regulation (EU) 2017/2402 laying down a general framework for securitisation and creating a specific framework for simple, transparent, and standardised securitisation (STS) creates a general framework for securitisation and introduces a special framework for STS. Regulatory instruments in various markets, such as CRR, Solvency II, and MMF, make reference to STS as regards securitisation, and among other things, provisions on securitisation have been transferred from CRR to the STS Regulation. The STS Regulation also amends CRR as regards prudential requirements, including risk models and capital ratios. Regulation (EU) 2021/557 amends Regulation (EU) 2017/2402 so as to support the post-COVID-19 economic recovery. It expands the STS framework to include additional types of securities and makes it easier to securitise non-performing exposures (NPE). A bill of legislation incorporating the Regulation into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### Regulation on Institutions for Occupational Retirement Provision (IORP II)

Directive (EU) 2016/2341 on the activities and supervision of institutions for occupational retirement provision (IORP II) sets forth rules on the establishment and operation of the activities carried out by IORPs. The previous Directive 2003/41/EC (IORP I) on the same topic has undergone a number of amendments; therefore, the Directive has been reissued. The purpose of the Directive is to ensure sound governance, provision

of information to fund members, and transparency and security of the occupational pension system so as to facilitate greater worker mobility between member states. A bill of legislation incorporating the Directive into Icelandic law is to be introduced before Parliament at the autumn 2024 legislative session. The bill would entail the passage of a new Act on Occupational Pension Funds and the repeal of the previous Act no. 78/2007 on the same topic, which was originally passed in order to implement the IORP I Directive.

#### Regulation on a pan-European personal pension product (PEPP)

Regulation (EU) 2019/1238 on a pan-European personal pension product (PEPP) entails a new voluntary type of pension savings that will be available to consumers within the EEA. The Regulation lays the groundwork for Europe-wide personal savings, where standardised core characteristics are guaranteed, such as transparency requirements, investment rules, and the right to switch products or investment types. This guarantees strong investor protection while giving product providers the flexibility to adapt the product to their own business model. A bill of legislation incorporating the Regulation into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### Regulation on digital operational resilience for the financial sector (DORA)

Regulation (EU) 2022/2554 on digital operational resilience for the financial sector (DORA) sets forth harmonised requirements for all financial system participants' information and communications technology (ICT) security, wherein they must ensure that they can withstand, respond to, and recover from any type of ICT disruption or cyberthreat. The main objective is to bolster companies' resilience, lower the frequency of cyberattacks, and reduce risk. Among other things, the Regulation lays down requirements pertaining to ICT risk management, reporting in connection with such risk, and testing and risk assessment in connection with outsourcing ICT services to a third party. Concurrently, Directive (EU) 2022/2556 provides for derived amendments to PSD II, IORP II, MIFID II, CRD IV, and AIFMD. A bill of legislation incorporating these instruments into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### Regulation on European crowdfunding service providers for business

Regulation (EU) 2020/1503 lays down harmonised requirements for provision, structure, authorisations,

operation, supervision, transparency, and marketing of crowdfunding services for businesses. Concurrently, Directive (EU) 2020/1504 provides for derived amendments to MiFID II. A bill of legislation incorporating these instruments into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### Regulation on cross-border payments in the European Union (CBPR)

Regulation (EU) 2021/1230 on cross-border payments codifies the provisions of Regulation (EC) no. 924/2009 on cross-border payments in the Union, specified provisions of Regulation (EU) no. 260/2012 establishing technical and business requirements for credit transfers and direct debits in euros and amending Regulation (EC) no. 924/2009, and the provisions of Regulation (EU) 2019/518 amending Regulation (EC) no. 924/2009. It is planned to pass new legislation on cross-border payments in euros and repeal Act no. 78/2014. One of the main changes from current law is that fees for cross-border payments in euros within the EEA are to be harmonised with fees for comparable payments in the domestic currency of the member state in which the provider of payment services is located. Another salient change is that the framework for information that payment service providers are obliged to disclose to customers on the cost of currency conversion prior to payment has been clarified. A bill of legislation incorporating the Regulation into Icelandic law is set for introduction at the autumn 2024 legislative session.

#### Review of EU banking regulations (CRD VI and CRR III)

In October 2021, the European Commission introduced its most recent proposal for revisions to the EU banking framework, referred to as *Banking Package 2021*. The package includes proposed amendments to Directive 2013/36/EU (CRD VI) and Regulation (EU) no. 575/2013 (CRR III). The aim of the Banking Package is to complete the incorporation of the Basel III standard into the EU banking framework. The package is intended to bolster banks' resilience. It also stipulates that banks must incorporate environmental, social, and governance factors more fully into their risk management, and supervisory bodies are granted additional powers to supervise banks and banking conglomerates. An agreement has been reached between the European Council and the European Parliament on the contents of the package, which will hopefully be approved formally by the EU in coming months. CRR III is expected to take effect within the EU in January 2025, and member states are expected to introduce the legislation and

directives necessary to ensure consistency with CRD VI within 18 months of the date the Directive takes effect within the EU.

# Appendices

## 1 Number of entities regulated by the Central Bank of Iceland Financial Supervisory Authority

Table 1 Number of regulated entities at the year-end

| Categories of regulated entities at each year-end              | 31.12.2018 | 31.12.2019 | 31.12.2020 | 31.12.2021 | 31.12.2022 | 31.12.2023 |
|--|------------|------------|------------|------------|------------|------------|
| Subject to licence or operating under special legislation:     |            |            |            |            |            |            |
| Commercial banks   | 4          | 4          | 4          | 4          | 4          | 4          |
| Savings banks  | 4          | 4          | 4          | 4          | 5          | 5          |
| Credit undertakings  | 5          | 5          | 4          | 3          | 4          | 4          |
| Housing Financing Fund (HFF)                                   | 1          | 0          | 0          | 0          | 0          | 0          |
| Investment firms   | 9          | 9          | 9          | 9          | 8          | 8          |
| UCITS management companies                                     | 9          | 9          | 9          | 6          | 6          | 6          |
| Alternative investment fund managers <sup>1</sup>              | 0          | 0          | 16         | 19         | 23         | 30         |
| Regulated markets (securities exchanges)                       | 1          | 1          | 1          | 1          | 1          | 1          |
| Central securities depositories                                | 2          | 2          | 1          | 1          | 1          | 1          |
| Pension funds <sup>2</sup>                                     | 21         | 21         | 21         | 21         | 21         | 21         |
| Insurance companies  | 11         | 11         | 11         | 10         | 10         | 10         |
| Insurance brokerages   | 7          | 8          | 9          | 9          | 9          | 9          |
| Entities with debt collection licences                         | 8          | 8          | 9          | 8          | 8          | 8          |
| Payment institutions   | 1          | 1          | 2          | 1          | 1          | 2          |
| Electronic money institutions                                  | 0          | 1          | 1          | 2          | 2          | 2          |
| Currency exchange services                                     | 1          | 1          | 1          | 1          | 0          | 0          |
| Guarantee funds  | 1          | 1          | 1          | 1          | 1          | 1          |
| Registered consumer mortgage loan providers                    | 1          | 1          | 0          | 0          | 0          | 0          |
| Virtual currency service providers                             | 1          | 1          | 3          | 3          | 3          | 4          |
| <b>Total</b>   | <b>87</b>  | <b>88</b>  | <b>106</b> | <b>103</b> | <b>107</b> | <b>116</b> |
| Other regulated entities:                                      |            |            |            |            |            |            |
| UCITS funds  | 40         | 37         | 37         | 36         | 38         | 38         |
| Alternative investment funds for retail investors <sup>3</sup> | 60         | 54         | 61         | 69         | 72         | 76         |
| Other alternative investment funds <sup>4</sup>                | 117        | 114        | 116        | 121        | 137        | 131        |
| Pension savings custodians <sup>5</sup>                        | 8          | 8          | 8          | 8          | 8          | 8          |
| Issuers of listed shares                                       | 23         | 24         | 23         | 26         | 30         | 31         |
| Issuers of listed bonds  | 50         | 57         | 51         | 51         | 56         | 62         |
| Registered consumer loan providers and brokers <sup>6</sup>    | 0          | 0          | 5          | 9          | 9          | 8          |
| Holding companies <sup>7</sup>                                 | 6          | 5          | 6          | 5          | 5          | 4          |
| Financial conglomerates <sup>8</sup>                           | 0          | 0          | 1          | 1          | 1          | 1          |
| <b>Total</b>   | <b>391</b> | <b>387</b> | <b>414</b> | <b>429</b> | <b>463</b> | <b>475</b> |

1. Including 12 licensed management companies, 6 of which are also UCITS management companies; and 18 registered entities, one of which is an investment firm.

2. Many pension funds are divided into divisions. There were 69 divisions at year-end 2023.

3. Previously investment funds.

4. Previously institutional investment funds.

5. Commercial banks and savings banks. Pension funds and foreign custodians are not included.

6. Supervised only pursuant to the Act on Measures against Money Laundering and Terrorist Financing.

7. Holding companies in the financial or insurance sector, or mixed holding companies.

8. Financial conglomerates in the financial or insurance sector.

Source: Central Bank of Iceland.

## 2 Activities of foreign entities in Iceland

Table 1 Number of foreign entities licensed to provide service in Iceland

| Number at year-end   | 2022        | 2023        |
|--|-------------|-------------|
| Credit institutions and financial institutions without establishments/branches                                     | 248         | 261         |
| UCITS (no. of subsidiary funds)  | 135 (1,353) | 131 (1,383) |
| Investment firms with business establishments/branches<br>(no. of establishments/branches)                         | 1 (1)       | 1 (1)       |
| Investment firms without establishments/branches   | 605         | 621         |
| Central securities depositories with business establishments/branches<br>(no. of establishments/branches)          | 1 (1)       | 1 (1)       |
| Central securities depositories without establishments/branches  | 6           | 6           |
| Insurance companies with establishments/branches<br>(no. of establishments/branches)                               | 2 (1)       | 2 (1)       |
| Insurance companies without establishments/branches  | 357         | 379         |
| Insurance brokers with establishments/branches<br>(no. of establishments/branches)                                 | 2 (2)       | 2 (2)       |
| Insurance brokers and insurance agents without establishments/branches   | 2,863       | 2,956       |
| Payment institutions with agents (no. of agents)   | 2 (3)       | 2 (3)       |
| Electronic money institutions with distributors (no. of distributors)  | 0           | 0           |
| Payment institutions and electronic money institutions without<br>establishments/branches                          | 384         | 420         |
| Credit intermediaries without establishments/branches  | 4           | 2           |
| Alternative investment fund managers without establishments/branches   | 162         | 176         |
| Number of companies registered outside the EEA and authorised to<br>provide services in Iceland under national law |             |             |
| Alternative investment fund managers (no. of funds)  | 42 (86)     | 44 (94)     |

Source: Central Bank of Iceland.



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