

Notification template for Article 131 CRD – Other Systemically Important Institutions (O-SII)

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1. Notifying national authority			
1.1 Name of the notifying authority	The Financial and Capital Market Commission (FCMC)		
2. Description of the measure			
2.1 Concerned institution or group of institutions	Bank name	LEI code	
	Luminor Bank AS	213800LDOTKJMCUB1M79	
	"Swedbank" AS	549300FXBIWWGK7T0Y98	
	AS "SEB banka"	549300YW95G1VBBGGV07	
	Akciju sabiedrība "Citadele banka"	2138009Y59EAR7H1UO97	
	Akciju sabiedrība "Rietumu Banka"	2138007F5HA5FFJROB80	
2.2 Level of the buffer applied	Bank name	O-SII buffer from 30 June 2019	
	Luminor Bank AS	2%	
	"Swedbank" AS	2%	
	AS "SEB banka"	1.75%	
	Akciju sabiedrība "Citadele banka"	1.5%	
	Akciju sabiedrība "Rietumu Banka"	1.25%	
The O-SII buffer requirement applied to the identified O-SIIs listed above is to be met by CET1 capital instruments and shall be maintained at the highest consolidation level in Latvia. Compared to the assessment in 2017 ABLV Bank AS is no longer identified as O-SII as its licence was withdrawn in July 2018. The buffer rates of AS "SEB banka" and Akciju sabiedrība "Rietumu Banka" are to be decreased by 0.25% compared to those currently applied as majority of the data points underlying the mandatory indicator values for these banks have decreased since last year.			
2.3 Name of the EU ultimate parent institution	Bank name	Parent company name	Parent company LEI code
	"Swedbank" AS	Swedbank AB	M312WZV08Y7LYUC71685
	AS "SEB banka"	Skandinaviska Enskilda Banken AB	F3JS33DEI6XQ4ZBPTN86
	Luminor Bank AS	Luminor Group AB	2138003BL9H2NAQXYD8

2.4 Names of subsidiaries	Bank name	Subsidiary name (country)	Subsidiary LEI code
	Akciju sabiedrība "Citadele banka"	AB "CITADELE" BANKAS (Lithuania)	213800YB53A7DY5ONR39

3. Timing of the measure	
3.1 Timing of the Decision	The FCMC is expected to take its final decision on 27 November 2018
3.2 Timing of the Publication	The decision will be published within 5 working days after the decision is taken.
3.3 Disclosure	The decision will be published on the website of the FCMC and letters will be sent to the identified O-SIIs informing them of this decision
3.4 Timing of Application	30.06.2019
3.5 Phasing in	The phase-in period of the O-SII buffer in Latvia ended on 30.06.2018
3.6 Review of the measure	The list of the identified O-SIIs and the O-SII buffer rates will be reviewed on an annual basis.

4. Reason for O-SII identification and activation of the O-SII buffer	
4.1 Scores of concerned institution or group of institutions, as per EBA guidelines on the assessment of O-SIIs (Article 131.3)	The relevant information is provided in the Excel file attached below the notification.
4.2 Methodology and indicators used for designation of the O-SII (Article 131.3)	The O-SII identification was performed according to the mandatory criteria and indicators, data definitions and calculation procedures specified in the EBA guidelines on the assessment of O-SIIs; however, two institutions above the relevant threshold (set at 425 bps since 2015 due to the size and specificities of the financial sector) were not identified as O-SIIs due to exercise of the supervisory judgement (see below), which is not fully consistent with the EBA guidelines. No optional indicators have been used and entities with total assets not in excess of 0.02% of the whole sample have not been excluded. Non-bank institutions have not been included in the calculations as they are relatively small and are of no systemic importance in the Latvian financial system. The calculations were based on the 2018Q2 FINREP data; when relevant FINREP data were unavailable, proxies were used from additional data available to the FCMC. Indicator values are provided in the Excel file attached below the notification.
4.3 Supervisory judgement	Due to significant structural changes in the Latvian financial sector in 2018 supervisory judgement had to be used in the identification of O-SIIs. In July 2018 the licence of ABLV Bank (which was identified as an O-SII in 2017 with the highest O-SII score in Latvian banking sector) was withdrawn as bank decided to apply for a voluntary liquidation following the statement released on February 13 by the US Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) naming the bank as the institution of primary money laundering concern and proposing Section 311 special measure. Furthermore, the ABLV Bank situation prompted an outflow of foreign client deposits from other banks with business models oriented towards servicing foreign clients. Meanwhile, concerted effort has been

undertaken by the parliament, regulators and banking sector participants to re-orient banks with high reliance on foreign clients' deposits to other business models. As a result, the size of the Latvian banking sector has significantly decreased in the first three quarters of 2018 - from 105% to 75% of GDP.

These developments have impacted the O-SII identification process in two major ways. Firstly, the decline in the size of the banking sector has mechanically resulted in increased O-SII scores of remaining participants (as the total of O-SII scores of all entities included in the calculation according to the EBA guidelines methodology is by definition equal to 10 000). Secondly, ABLV Bank was the largest issuer of outstanding debt securities in Latvian banking sector (estimated as 69% of sector total during the 2017 O-SII identification exercise). Reliance of Latvian banks on this financing channel has historically been non-significant as banking sector has been dominated by subsidiaries and branches of other EU institutions (65% in terms of total assets as of 2018Q2). The withdrawal of ABLV Bank licence in concert with the decision of another large bank to cease issuance has resulted in a further decrease of outstanding debt securities issued by the banking sector from 2.6% of Latvian GDP as of 2017Q2 to 0.6% of GDP in 2018Q2. At the same time this indicator is assigned a weight of 8.33% according to the EBA methodology, which is a substantial mismatch compared to the systemic importance of issuance of outstanding debt securities in Latvian financial sector.

Hence, a straightforward application of the EBA methodology would result in identification as O-SIIs of two additional banks based purely on the contribution of the outstanding debt securities indicator:

Bank name	2018 O-SII score*	2018 O-SII score without the contribution of outstanding debt securities indicator	2017 O-SII score
AS BlueOrange Bank	564	350	245
AS "NORVIK BANKA"	530	329	381

* the threshold for O-SII identification is set at 425 bps

The issuance of outstanding debt securities in these two banks as of 2018Q2 does not exceed 50 million EUR, therefore to identify them as O-SIIs based on the contribution of this indicator would be inappropriate in view of their true systemic importance in the Latvian financial system. Furthermore, the reduction of the size of Latvian banking sector has further mechanically inflated the O-SII scores of these two banks – both of them actually saw a decrease in asset size in a period from 2017Q2 to 2018Q2, as well as decrease in the underlying data values behind the majority of other indicators:

Bank name	Change in total assets 2017Q2 to 2018Q2	Number of indicators, for which in period from 2017Q2 to 2018Q2 the underlying data values		
		increased	decreased	did not change
AS BlueOrange Bank	-7.5%	3	6	1
AS "NORVIK BANKA"	-40.3%	1	9	0

On these grounds the FCMC has decided to exercise its supervisory judgement and not to identify AS BlueOrange Bank and AS "NORVIK BANKA" as O-SIIs despite their O-SII score being above the threshold of 425 bps according to the calculation made in line with the mandatory indicators and methodology of the EBA guidelines.

4.4 Calibrating the O-SII buffer

The calibration was based on the *equal expected impact* method wherein the size of the O-SII buffers is set with aim to equalize the expected impact of an O-SIIs' financial distress with the expected impact of a non-O-SII reference institution's financial distress.

In line with the chosen threshold used for O-SII identification, systemic importance score of 425 basis points was used to define a non-O-SII reference institution. For

purposes of calibrating the O-SII buffer, the systemic importance scores have since 2016 been calculated by employing an adjusted EBA Guidelines' methodology which takes into account the specificities of national financial sector. Due to the previously highlighted major changes in the size and structure of the Latvian banking sector, in particular, the decrease of the outstanding stock of debt securities issues by the banking sector and the reorientation from foreign to local clients, the weighting of indicators used for the O-SII buffer calibration has been changed in 2018 as per the table below:

Criterion	Indicators	EBA guidelines weights	Adjusted methodology for buffer calibration weights (2016-2017)	Adjusted methodology for buffer calibration weights (2018-)
Size	Total assets	25%	25%	25%
	Risk weighted assets		15%	15%
Importance (including substitutability/financial system infrastructure)	Value of domestic payment transactions	8.33%	5%	5%
	Private sector deposits from depositors in the EU	8.33%	5%	5%
	Private sector loans to recipients in the EU	8.33%	5%	5%
	Private sector deposits from Latvian residents		5%	7.5%
	Private sector loans to Latvian residents		5%	7.5%
	Credit risk stress test – additional provisions (% of total provisions needed in banking sector)			5%
Complexity/cross-border activity	Value of OTC derivatives (notional)	8.33%	5%	5%
	Cross-jurisdictional liabilities	8.33%	5%	5%
	Cross-jurisdictional claims	8.33%	5%	5%
Interconnectedness	Intra-financial system liabilities	8.33%	5%	4.5%
	Intra-financial system assets	8.33%	5%	4.5%
	Debt securities outstanding	8.33%	5%	1%

The decision to slightly decrease the weightings of intra-financial system liabilities and assets indicators is motivated by the decrease of importance of those indicators for determining the banks' systemic importance in Latvian financial system – the sector-wide sum total of the data underlying both these indicators has decreased from 30% of GDP as of 2017Q2 to 17% of GDP in 2018Q2.

In order to achieve an equal expected impact of financial distress, the probability of default (PD) of financial distress of O-SII must be lower than that of non-O-SII, as financial distress of O-SIIs leads to higher associated economic costs. These costs are decreased by applying O-SII buffers that lower PDs of O-SIIs.


Quarterly data for period of 2004-2017 on return on risk weighted assets (RORWA) of banks operating in Latvia were used to determine the PD of a reference non-O-SII.

4.5 Effectiveness and proportionality of measure

The higher capital requirements resulting from the application of the O-SII buffer are essential to ensure the resilience of the systemically important institutions in Latvia. The total assets of the identified O-SIIs account for around 82% of Latvian banking sector assets and approximately 63% of Latvian GDP as of 2018Q2 – financial distress of these institutions would negatively affect financial stability and economy of Latvia.

As of 2018Q2, identified O-SIIs already fulfil the total capital and buffer requirements

	with the CET1 capital and the level of the buffer has not increased for any bank therefore the decision to implement the O-SII buffer should not cause any disruptions to the local financial system or economy.		
5. Cross-border and cross-sector impact of the measure			
5.1 Assessment of cross-border effects and the likely impact on the internal market (Recommendation ESRB/2015/2)	The cross-border effects and impact on the internal market is expected to be nonmaterial as the EU parent institutions of local subsidiaries identified as O-SIIs are required to hold at least as large O-SII buffers on the consolidated level as FCMC is planning to set in Latvia, and cross-border activities within EU of identified O-SIIs are limited.		
5.2 Assessment of leakages and regulatory arbitrage within the notifying Member State	As the measure is institution-specific, possibility of any leakages is minimal.		
6. Combinations and interactions with other measures			
6.1 Combinations between G-SII and O-SII buffers (Article 131.14)	N/A		
6.2 Combinations with SRB buffers (Article 131.14 + Article 133.5)	N/A		
6.3 O-SII requirement for a subsidiary (Article 131.8)	Bank name	Parent company name	O-SII buffer rate of parent company
	"Swedbank" AS	Swedbank AB	2%
	AS "SEB banka"	Skandinaviska Enskilda Banken AB	2%
	Luminor Bank AS	Luminor Group AB	
6.4 Interaction with other measures	N/A		

7. Miscellaneous	
7.1 Contact person(s) at notifying authority	Arnis Jankovskis (Senior regulations expert, Regulations Division, +371 6777 904, arnis.jankovskis@fktk.lv)
7.2 Any other relevant information	<div style="text-align: center;">  Annex_LV_FCMC_O-SII_identification_201 </div> <p>Excel file referred in 4.1 and 4.2: N.B. The information in this file can be shared with other authorities but should</p>

	not be made publicly available.
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