

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

Please send this template to

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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	
	"Swedbank" AS	549300FXBIWVGK7T0Y98	
	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 2020	
	"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 2018 Luminor Bank AS is no longer identified as O-SII as starting from 02.01.2019 it continues its operations as the Latvian branch of Luminor Bank AS which is licensed in Estonia. The buffer rates of four identified O-SIIs remain unchanged compared to the 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
2.4 Names of subsidiaries	Bank name	Subsidiary name (country)	Subsidiary LEI code
In 2018 notification the Lithuanian subsidiary of Akciju sabiedrība "Citadele banka"			

	was included, however as of 02.01.2019 it has changed its status to a branch.
3. Timing of the measure	
3.1 Timing of the Decision	The FCMC is expected to take its final decision on 26.11. 2019
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 the decision
3.4 Timing of Application	30.06.2020
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, in a similar vein as last year, one institution above the relevant threshold (set at 425 bps since 2015 due to the size and specificities of the financial sector) was 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 2019Q2 FINREP data; for data not incorporated in FINREP proxies were used from additional data sources available to the FCMC. Indicator values are provided in the Excel file attached below the notification.
4.3 Supervisory judgement	<p>Due to ongoing changes in the structure of Latvian financial sector since 2018, same as last year the supervisory judgement had to be used again in the identification of O-SIIs.</p> <p>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. ABLV Bank was at that time the largest issuer of debt securities in Latvian banking sector (estimated at 69% of sector total during the 2017 O-SII identification exercise).</p> <p>Furthermore, the European Central bank (ECB) as a direct supervisor of JSC "PNB Banka" decided on 2019.08.15 to recognize the bank as failing or likely to fail financial institution; on the same day the Board of the FCMC at an extraordinary</p>

meeting decided to suspend the provision of financial services by the bank. JSC “PNB Banka” was at that time the third largest issuer of debt securities in Latvian banking sector (estimated at 24% of sector total during the 2018 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 (67% in terms of total assets as of 2019Q2). The exit of ABLV Bank and JSC “PNB Banka” from the market in subsequent years has resulted in a further decrease of outstanding debt securities issued by the banking sector from 2.6% of Latvian GDP in 2017Q2 to 0.6% of GDP in 2018Q2 to 0.4% of GDP in 2019Q2. 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 the actual issuance of outstanding debt securities in Latvian financial sector.

Hence, a straightforward application of the EBA methodology in 2018 and this year would have had resulted in the identification of AS BlueOrange Bank as O-SII 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	2019 O-SII score*	2019 O-SII score without the contribution of outstanding debt securities indicator
AS BlueOrange Bank	564	350	531	290

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

The amount of outstanding debt securities of AS BlueOrange Bank as of 2019Q2 does not exceed 50 million EUR, therefore to identify it as O-SIIs based on the contribution of this indicator would be inappropriate in view of bank’s true systemic importance in the Latvian financial system.

On these grounds, as in 2018, the FCMC has decided to exercise its supervisory judgement and not to identify AS BlueOrange Bank as O-SIIs despite its 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. In 2018 the weighting of adjusted indicators used for the O-SII buffer calibration was changed (see the table below) due to the decrease in the outstanding stock of debt securities issued by the banking sector (see 4.3) and significant structural changes in the Latvian financial sector. The previously highlighted ABLV Bank situation prompted an outflow of foreign client deposits from other banks with business models oriented towards servicing foreign clients. Meanwhile, concerted effort was 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 – from 105% of GDP at the beginning of 2018 to 75% in 2018Q3 to 70% in 2019Q2. The decision to also slightly decrease the weightings of intra-financial system liabilities and assets indicators in 2018 was motivated by the decrease of importance of those indicators for determining the banks' systemic importance in Latvian financial system – the sector-

	<p>wide sum total of the data underlying both these indicators has decreased from 30% of GDP in 2017Q2 to 17% of GDP in 2018Q2 to 15% in 2019Q2.</p> <p>For this year's calculation there have been no further changes to the adjusted indicators used for the O-SII buffer calibration.</p> <table border="1" data-bbox="548 327 1399 1136"> <thead> <tr> <th>Criterion</th> <th>Indicators</th> <th>EBA guidelines weights</th> <th>Adjusted methodology for buffer calibration weights (2016-2017)</th> <th>Adjusted methodology for buffer calibration weights (2018-)</th> </tr> </thead> <tbody> <tr> <td rowspan="2">Size</td> <td>Total assets</td> <td>25%</td> <td>25%</td> <td>25%</td> </tr> <tr> <td>Risk weighted assets</td> <td></td> <td>15%</td> <td>15%</td> </tr> <tr> <td rowspan="6">Importance (including substitutability/financial system infrastructure)</td> <td>Value of domestic payment transactions</td> <td>8.33%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td>Private sector deposits from depositors in the EU</td> <td>8.33%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td>Private sector loans to recipients in the EU</td> <td>8.33%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td>Private sector deposits from Latvian residents</td> <td></td> <td>5%</td> <td>7.5%</td> </tr> <tr> <td>Private sector loans to Latvian residents</td> <td></td> <td>5%</td> <td>7.5%</td> </tr> <tr> <td>Credit risk stress test – additional provisions (% of total provisions needed in banking sector)</td> <td></td> <td></td> <td>5%</td> <td>5%</td> </tr> <tr> <td rowspan="3">Complexity/cross-border activity</td> <td>Value of OTC derivatives (notional)</td> <td>8.33%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td>Cross-jurisdictional liabilities</td> <td>8.33%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td>Cross-jurisdictional claims</td> <td>8.33%</td> <td>5%</td> <td>5%</td> </tr> <tr> <td rowspan="3">Interconnectedness</td> <td>Intra-financial system liabilities</td> <td>8.33%</td> <td>5%</td> <td>4.5%</td> </tr> <tr> <td>Intra-financial system assets</td> <td>8.33%</td> <td>5%</td> <td>4.5%</td> </tr> <tr> <td>Debt securities outstanding</td> <td>8.33%</td> <td>5%</td> <td>1%</td> </tr> </tbody> </table> <p>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.</p> <p>Quarterly data for period of 2004-2018 on return on risk weighted assets (RORWA) of banks operating in Latvia were used to determine the PD of a reference non-O-SII.</p>	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%	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%
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<p>4.5 Effectiveness and proportionality of measure</p>	<p>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 66% of Latvian banking sector assets and 47% of Latvian GDP as of 2019Q2 – financial distress of these institutions would negatively affect financial stability and economy of Latvia.</p> <p>As of 2019Q2, identified O-SIIs fulfil the buffer requirements with the CET1 capital and as the level of the buffer has not increased for any bank no resulting disruptions to the local financial system or economy are expected.</p>																																																																		
<p>5. Cross-border and cross-sector impact of the measure</p>																																																																			
<p>5.1 Assessment of cross-border effects and the likely impact on the internal market (Recommendation ESRB/2015/2)</p>	<p>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.</p>																																																																		

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)	<table border="1"> <thead> <tr> <th>Bank name</th> <th>Parent company name</th> <th>O-SII buffer rate of parent company</th> </tr> </thead> <tbody> <tr> <td>"Swedbank" AS</td> <td>Swedbank AB</td> <td>2%</td> </tr> <tr> <td>AS "SEB banka"</td> <td>Skandinaviska Enskilda Banken AB</td> <td>2%</td> </tr> </tbody> </table>	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%
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AS "SEB banka"	Skandinaviska Enskilda Banken AB	2%								
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;">  O-SII_data.xlsx </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 not be made publicly available.</p>