Notification template for borrower-based measures

Please send/upload this template to:

- macropru.notifications@ecb.europa.eu when notifying the European Central Bank (ECB);
- DARWIN/ASTRA when notifying the European Systemic Risk Board (ESRB).

This notification will be made public by the ESRB once the relevant authorities have adopted and published the notified macroprudential measure[1].

E-mailing/uploading this template to the above addresses constitutes official notification; no further official letter is required. In order to facilitate the work of the notified authorities, please send the notification template in a format that allows the information to be read electronically.

1. Notifying national authority and scope of the notification		
1.1	Name of the notifying authority	Central Bank of Iceland
1.2	Country of the notifying authority	Iceland
1.3	Type of borrower-based measure	Please select one of the measures listed below: ☒ Debt-service-to-income (DSTI) ☐ Loan-to-income (LTI) ☒ Loan-to-value (LTV) ☐ Debt-to-income (DTI) ☐ Loan maturity ☐ Other (please provide a short, name-like description here and provide more details in Section 2)
1.4	Type of notification	What do you intend to notify? ☐ Activation of a new measure ☒ Change to an existing measure ☐ Extension of an existing measure ☐ Termination of an existing measure

[1] On request by the notifying authority, it may be agreed with the Head of the ESRB Secretariat that this notification, or a part thereof, should not be published for reasons of confidentiality or financial stability.

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2. Description of the measure		
2.1	Description of the measure	Rules on maximum LTV changed: • Maximum LTV for first-time buyers decreased from 90% to 85%. • Maximum LTV for other buyers maintained at 80%. Rules on maximum DSTI changed: • When calculating debt service in accordance with the rules the higher of contractual interest rates or a reference interest rate of 3% for indexed mortgages and 5.5% for non-indexed mortgages should be used. • When calculating debt service in accordance with the rules, the maximum maturity is 25 years for indexed mortgage loans (was previously 30 years) and 40 years for non-indexed mortgage loans (unchanged). • When calculating debt service in accordance with the rules the lender is authorised to use an annuity mortgage amortisation schedule for both indexed and non-indexed mortgage loans. Otherwise, the DSTI rules remain unchanged, maximum Debt-Service-to-Income limit of 35% applies to all new mortgage lending to consumers. In case of first-time buyers, the maximum limit is 40%. The debt service includes all payments of principal and interest of all mortgage loans of the consumer. Income of the consumer is defined as long term sustainable income net of taxes, pension contributions and other deductions. The DSTI rules provide for a flexibility quota of 5% of the volume of new mortgages each quarter that are exempt from the rules. Refinancing of mortgage loans due to payment difficulties of the consumer is exempt from the DSTI rules.
2.2	Definition of the measure	Rules on a maximum Loan-to-Value: • (Loan) is defined as the sum of all mortgage loans secured by a specific residential property. • (Value) is defined as the market value of the same residential property. If the market value according to a purchase agreement is not available, e.g. in the case of refinancing, the property valuation from Registers Iceland is used. • These rules only apply to mortgage loans to consumers and residential real estate as defined by law no. 118/2016 on mortgages to consumers. Rules on maximum Debt-Service-to-Income

		• (Debt-Service) includes all payments of principal and interest of all mortgage loans of the consumer calculated in accordance with Article 5 of the rules (higher of contractual interest rate and minimum interest rate, maximum maturity and . • (Income) of the consumer is defined as long term sustainable income net of taxes, pension contributions and other deductions. Income is assessed in accordance with regulation no. 270/2017 on mortgages to consumers, ensuring income is assessed in a consistent manner by all lenders as well as other factors relevant to the creditworthiness of consumers.
2.3	Legal basis and process of implementation of the measure	Borrower based measures are implemented by issuing legally binding rules based on Chapter VII of law no. 118/2016 on mortgages to consumers. The Central Bank of Iceland issues the rules following approval by the Financial Stability Committee (i. Fjármálastöðugleika-nefnd, FSN). Violation of the rules is subject to fines.
2.4	Coverage	All institutions operating in the Icelandic housing mortgage market, including banks, pension funds, the Housing and Construction Authority and other registered lenders. Institutions that intent to extend mortgage credit to consumers are obliged by Article 42 of law no. 118/2016 to register with the Financial Supervisory Authority of the Central Bank of Iceland prior to starting operations.
		The law, and therefore the rules, apply to consumers (natural persons) only.
		The law, and therefore the rules, apply to mortgage credit to consumers (natural persons) only.

2.5	Calibration	The calibration of the lower LTV limit for first-time buyers was in line with the increased overvaluation in the RRE market. Calibration of the reference interest rates is in accordance with an estimate of the equilibrium real interest rate. Intended to limit excessive mortgage lending at unsustainably low interest rates. To improve effectiveness of the DSTI rules, the calibration also intends to reduce the difference in calculated debt-service of different mortgage types (indexed and non-indexed).
	3. Timing for the measure	
3.1	Timing for the decision	What is the date of the official decision of the notified measure? 15/06/2022
3.2	Timing for publication	What is the date of publication of the notified measure? 15/06/2022
3.3	Disclosure	The decision to implement the rules has been presented in a press release on 15 June 2022: • https://www.cb.is/publications/news/news/2022/06/15/Statement-of-the-Financial-Stability-Committee-14-June-2022/ The rules are published in the Official Journal of Iceland: • New LTV rules: https://www.stjornartidindi.is/Advert.aspx?RecordID=c9a53dc2-7afc-4066-8e0f-3968b8c976d5 • New DSTI rules: https://www.stjornartidindi.is/Advert.aspx?RecordID=045933fe-d5d8-4b69-a416-010b92000550
3.4	Timing for the application	What is the intended date for application of the measure? What is the intended timeline for phase-in of the measure, if relevant? 16/06/2022

3.5	End date (if applicable)	Until when is it presumed that the measure will be in place? If applicable, please give an end date. N/A
4. Reason for activation of the measure		
4.1	Description of the macroprudential risk	Real estate prices have risen still higher this year and have deviated noticeably from fundamentals such as wages, building costs, and rent prices. In order to safeguard the resilience of borrowers and lenders alike, and in view of the current circumstances, the Financial Stability Committee (FSN) has decided to lower the maximum loan-to-value (LTV) ratio on mortgage loans to first-time buyers from 90% to 85%. The maximum LTV ratio is held unchanged for other buyers. The Committee has also decided to establish a reference interest rate for the calculation of debt service in the Rules on Maximum Debt Service-to-Income Ratios for Mortgage Loans to Consumers. The reference rate will be a minimum of 3% for indexed mortgages and 5.5% for non-indexed mortgages. Furthermore, the FSN has decided to shorten the maximum loan term used to calculate debt service on indexed loans to 25 years. The changes in the debt service-to-income (DSTI) ratio are intended to increase borrowers' risk awareness when they select from among loan types, as the debt service burden on indexed loans is relatively lighter early on and then grows heavier over the term of the loan. The objective of the above-specified measures is to limit the accumulation of systemic risk in the financial system.
4.2	Indicators used for activation of the measure	When evaluating systemic risk in the housing market a wealth of indicators are used. These include but are not limited to: Real house prices and housing market turnover in greater Reykjavík Real house prices and housing market turnover outside greater Reykjavík Real house prices in greater Reykjavík, deviation from trend Various housing market indicators, such as average time-to-sale, no. of apartments sold above asking price, no. of apartments listed for sale. Capital area house prices and their determinants (e.g., building cost, income, rent) GSADF test of price developments Fully finished new flats in greater Reykjavík Household credit growth

		Household credit-to-GDP ratio Consumer mortgages, by type Developments in mortgage lending rates Developments in LTV ratios of new consumer mortgages Developments in DSTI ratios of new consumer mortgages
4.3	Effects of the measure	The measure is designed to have modest direct effect on the mortgage market at this time but limits the risk that increasing house prices and deviation from income could lead to a deterioration of lending standards. The changes to the DSTI rules are designed to reduce incentives of borrowers to take on indexed mortgage loans at unsustainable interest rates in the medium to long term. The measure is designed to have medium to long term effects on the mortgage and housing markets, promoting stability, limiting build-up of systemic risk and strengthening resilience of borrowers and lenders.
5. Sufficiency, consistency and non-overlap of the policy response		
5.1	Sufficiency of the policy response	In general, the measure is designed to have medium to long term effects on the mortgage and housing markets, promoting stability, limiting build-up of systemic risk and strengthening resilience of borrowers and lenders. The specific changes to the rules at this time specifically target weaknesses identified: 1. the potential risk of high LTV lending to first-time buyers at a time when housing prices have deviated from fundamentals and there is increased risk of a price correction 2. the potential risk of increased household indebtedness by taking on indexed mortgage at, in the long run, unsustainable interest rates.

5.2	Consistency of application of the policy response	The macroprudential policy response is consistent with intermediate objective (1) to mitigate and prevent excessive credit growth and leverage, specifically of households during a time of an exuberant housing market that has increased overall systemic risk in Iceland during the past couple of years.
5.3	Non-overlap of the policy response	The borrower-based measures calibrated at this time are designed to target specific weaknesses that have been identified. The use of both LTV and DSTI has been shown to increase resilience of both lenders and borrowers. The measures also target all lenders and borrowers and are therefore ideal to address the weaknesses identified. No other measures have been put in place to target these weaknesses.
6. Cross-border and cross-sector impact of the measure		
6.1	Assessment of cross-border effects and the likely impact on the Internal Market	The measure applies to domestic mortgage loans granted by all mortgage lenders in Iceland. At present only domestic financial institutions operate in the Icelandic mortgage market. Cross border effects are therefore limited and no impact expected on the internal market.

	(Recommendation ESRB/2015/2[2])	
6.2	Assessment of leakages and regulatory arbitrage within the notifying Member State	The measure applies to all mortgage lenders in Iceland, including banks, pension funds, the Housing and Construction Authority and other registered lenders. Therefore, the scope for leakages and regulatory arbitrage is very limited.
6.3	Request for reciprocation	No

[2] Recommendation of the European Systemic Risk Board of 15 December 2015 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures (ESRB/2015/3) (OJ C 97, 12.3.2016, p. 9).

6.4	Justification for the request for reciprocation	N/A
7. Miscellaneous		
7.1	Contact person(s)/mailbox at notifying authority	Contact person(s) (name, phone number and e-mail address) and mailbox for further inquiries. Mr. Einar Jón Erlingsson Phone number: +354 569 9600 E-mail address: einar.jon.erlingsson@sedlabanki.is Mr. Eggert Þröstur Þórarinsson Phone number: +354 569 9600 E-mail address: eggert.throstur.thorarinsson@sedlabanki.is
7.2	Any other relevant information	
7.3	Date of the notification	Please provide the date on which this notification was uploaded/sent. 16/06/2022