



FINANSTILSYNET

THE FINANCIAL SUPERVISORY
AUTHORITY OF NORWAY

European Banking Authority (EBA) att: Isabelle Vaillant
DEFENSE 4 – EUROPLAZA, 20 Avenue André Prothin
CS 30154, 92927 Paris La Défense CEDEX

OUR REFERENCE
22/2744

YOUR REFERENCE

CONFIDENTIAL

DATE
26.08.2022

Subject: CET1 eligibility – instruments issued by Norwegian institutions

Dear Ms Vaillant,

Reference is made to your letter dated 9 June 2022 and to previous correspondence, including our letter to EBA dated 3 March 2022.

EBA has assessed three types of CET1 instruments (ordinary shares, equity certificates and members' contribution) issued by Norwegian credit institutions in course of the process to add them to EBA CET1 list. EBA has identified certain issues which raise concern as to their compliance with the eligibility criteria set out in Article 28 of Regulation (EU) No 575/2013 (CRR) and Commission Delegated Regulation (EU) No 241/2014, in particular related to the 'minimum dividend' rule for ordinary shares in the Norwegian Public Limited Liability Companies Act (Section 8-4), some 'loss absorption' features for equity certificates, as well as aspects related to 'direct/indirect funding' and 'redemption rights' attached to some members' contributions.

In relation to the issues identified in the letter dated 9 June 2022, EBA has asked the Norwegian Financial Supervisory Authority (Finanstilsynet) to explain the remedial or mitigating actions possibly envisaged for the different types of instruments, with a corresponding tentative timeline, mindful of the fact that, while some of these steps might be processed in the short term, others might necessitate a longer time horizon.

Ordinary shares

Finanstilsynet has no comments to EBA's assessment of ordinary shares. To address EBA's concerns in relation to ordinary shares, Finanstilsynet will propose necessary amendments to the Public Limited Liability Companies Act to the Ministry of Finance.

Finanstilsynet has been given an assignment from the Ministry of Finance to consider and propose amendments to the legislation that applies to financial institutions. Finanstilsynet will include a

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proposal for amendments related to ordinary shares in the draft consultation document, which will be sent to the Ministry of Finance by the end of this year.

Equity certificates

Finanstilsynet refers to the communication in advance of the final assessment from EBA. As mentioned in this communication, the assessment of equity certificates is of great importance for the Norwegian banking sector as a majority of the banks are savings banks with equity certificates.

EBA has raised concerns regarding two issues relating to the capital structure of Norwegian savings banks that have issued equity certificates. Finanstilsynet comments on each of these issues below.

Loss absorption


Finanstilsynet acknowledges that it is necessary to look into the loss absorption mechanism of savings banks with equity certificates. However, it is not entirely clear how the legal framework should be amended in order to meet EBA's expectations, cf. the following statement in your letter: *'(..) it is necessary that the concerned institutions progressively increase their dividend equalization fund over time, in particular when it is at a level significantly lower than the ownerless capital'*. At the same time, the legal basis in the CRR for this statement is not entirely clear based on the reference to CRR Article 26 (1) and Article 28 (1) (i) in EBA's letter. Nevertheless, Finanstilsynet recognises that the assessment of equity certificates in relation to the CRR requirements is challenging due to the complexity of the regulations governing this instrument.

A significant change in the loss absorption mechanism for equity certificates will probably affect other parts of the regulation of equity certificates (like voting rights) and may have an impact on the capital structure of savings banks and ultimately on the structure of the Norwegian banking sector. Thus, there is a need to thoroughly assess possible remedial or mitigation actions related to the loss absorption mechanism of savings banks with equity certificates.

As other regulatory issues have recently been debated in relation to equity certificates, the Ministry of Finance stated in September 2021 that it will consider the regulation of these instruments and other regulatory issues affecting savings banks. The Ministry has not yet started this work. Finanstilsynet will send a letter to the Ministry of Finance proposing that the Ministry as soon as possible initiates a comprehensive assessment of the capital structure in the savings bank sector, which should include following up EBA's assessment of equity certificates and the legal reasoning behind this.

Since the issues concerning equity certificate capital are complex and need to be considered thoroughly, any amendments to the regulation will probably not be in place until 2024 at the earliest.

Finanstilsynet assumes that equity certificates will be included in the CET1 list published by EBA until the aforementioned assessment initiated by the Ministry of Finance has been completed and necessary legal amendments are in place.


Reduction of equity capital

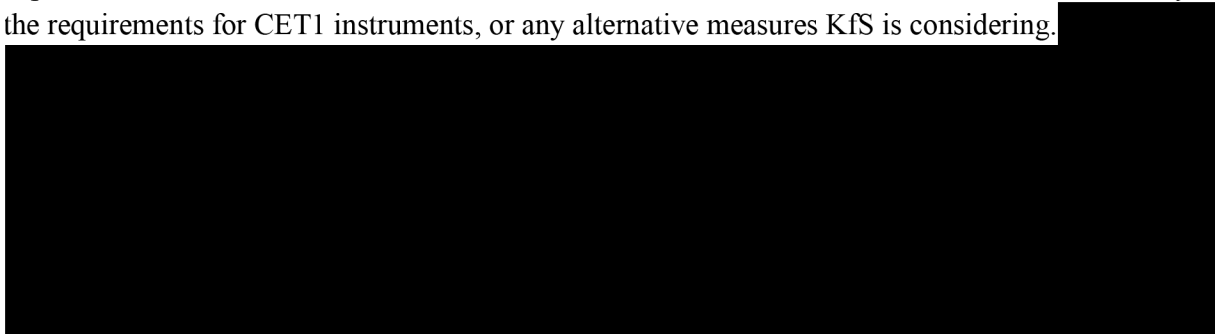
EBA concludes that the Financial Institutions Act does not explicitly require any reduction of the equity capital being subject to the competent authority's prior approval, and that it is necessary to amend the Financial Institutions Act.

Finanstilsynet has already proposed regulatory amendments to the Ministry of Finance in order to limit the possibility of reducing the dividend equalisation fund. Finanstilsynet has proposed restrictions on the right to transfer assets from the dividend equalisation fund – in the case of a bonus issue by making a transfer from the dividend equalisation fund to equity capital. In addition, Finanstilsynet has stated that it will consider proposing an amendment to section 10-18 of the Financial Institutions Act to clarify that the dividend equalisation fund cannot be reduced without Finanstilsynet's approval.

Finanstilsynet will suggest an amendment of the Financial Institutions Act to ensure that any reduction of equity capital shall be subject to the competent authority's prior approval. Finanstilsynet will include a proposal for necessary amendments in its draft consultation document, which will be sent to the Ministry of Finance by the end of the year.

Members' contributions in Kredittforeningen for Sparebanker

Finanstilsynet has an ongoing dialogue with Kredittforeningen for Sparebanker (KfS) regarding members' contributions. Finanstilsynet has asked the board of directors of KfS to provide an explanation of which measures KfS will consider in order for the members' contributions to satisfy the requirements for CET1 instruments, or any alternative measures KfS is considering.



Hopefully, EBA will find the mitigating actions described in this letter adequate in the short and medium term.

Yours sincerely,

Ann Viljugrein
Deputy Director General

Hege Bunkholt Elstrand
Head of Section

This document has been electronically approved and does not require handwritten signatures.