

Principles for identifying other systemically important credit institutions and setting their additional capital requirements

1 Background

Systemically important credit institutions are those that pose a systemic risk so great that, if realised, it would have a highly negative impact on the entire financial system and the real economy.

Systemically important credit institutions are typically large relative to other credit institutions, are functionally diverse, and have significant interlinkages, directly or indirectly, with the rest of the financial system and the economy. As a result, the solvency and liquidity problems of these institutions easily spread to the rest of the financial system. In the regulatory framework, systemic importance is examined globally (global systemically important banks, G-SIBs) and at the EU level as well as nationally (other systemically important institutions, O-SIIs).

The risks of systemically important credit institutions for the entire financial sector and the economy are mitigated by strengthening the institutions' loss absorbency, thereby reducing the probability of their failure. The objective of additional capital requirements imposed on O-SIIs (O-SII buffers) is to prevent macroprudential risks arising from structural factors in the financial markets.

2 Identification principles for O-SIIs and designation of Finnish O-SIIs

Under chapter 10, section 8 of the Act on Credit Institutions, national credit institutions significant for the financial system (i.e. other systemically important institutions, O-SIIs) refer to credit institutions

1. the balance sheet total of which is at least EUR 1 billion **and**
2. the insolvency of which would jeopardise the stability of the financial markets in Finland or in another EU Member State.

The Financial Supervisory Authority (FIN-FSA) is required to determine the group of O-SIIs on an annual basis. The designation of Finnish credit institutions as O-SIIs is based on the Guidelines of the European Banking Authority (EBA) on the criteria for the assessment of O-SIIs¹. O-SIIs are identified on the basis of the EBA Guidelines' four basic criteria and ten related indicators (Table 1). The indicators are normalised by dividing the indicator value of each individual credit institution by the sum of the respective indicator values of all credit institutions in the Member State (incl. branches).

In accordance with the EBA Guidelines, O-SIIs are determined in a two-step procedure:

1. Institutions whose overall O-SII score – calculated as the weighted average of indicator-specific scores – is equal to or over 3.5% are automatically designated as O-SIIs. The national macroprudential authority may adjust the threshold to

¹ [EBA/GL/2014/10](#).

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take into account the specificities of the national credit institutions sector and the statistical distribution of the scores. This aims to ensure the homogeneity of the group of O-SIIs in terms of the O-SIIs' systemic importance. National discretion is 0.75 percentage points in each direction.

2. Macroprudential authorities should assess whether institutions other than those identified in the first step should be designated as O-SIIs. This assessment should be based on the mandatory or optional indicators specified in the Annexes to the EBA Guidelines.

In determining O-SIIs, the FIN-FSA also applies the balance sheet total threshold of EUR 1 billion laid down in chapter 10, section 8 of the Act on Credit Institutions. Credit institutions with an overall O-SII score equal to or less than 0.045% in the first step of the O-SII assessment are also not designated as O-SIIs when applying supervisory judgment in step two.

Table 1. Criteria and indicators applied in the identification of O-SIIs²

Criteria	Indicators	Weight
Size	Balance sheet total (total assets)	25%
Importance/substitutability	Value of domestic payment transactions	8.33%
	Private sector deposits from depositors in the EU	8.33%
	Private sector loans to recipients in the EU	8.33%
Interconnectedness	Intra-financial system liabilities	8.33%
	Intra-financial system assets	8.33%
	Debt securities outstanding	8.33%
Complexity	Value of OTC derivatives (notional)	8.33%
	Cross-jurisdictional liabilities	8.33%
	Cross-jurisdictional claims	8.33%

Following the redomiciliation of Nordea Bank Abp to Finland in 2018, the quantified relative importance of other credit institutions decreased substantially although their risk positions, the nature and scope of their activities and their absolute importance remained unchanged. To ensure that the systemic importance of O-SIIs is assessed in a consistent manner and that the group of O-SIIs remains homogeneous, the FIN-FSA lowered the threshold of systemic importance from 3.5% to 2.75% in connection with its O-SII decisions of 2018.

² In interpreting the calculations and indicators, the following factors should be taken into account:

- All the indicators are based on FINREP reporting data, except for the indicator of payment transactions, which is based TARGET payment transactions data.
- The calculations do not include insurance business items.
- Private sector deposits from depositors in the EU: credit institutions whose foreign liabilities account for less than 10% of balance sheet liabilities do not report deposits from depositors in the EU separately. With respect to these institutions, the figure includes all deposits.
- Private sector loans to recipients in the EU: credit institutions whose foreign claims account for less than 10% of balance sheet assets do not report loans to recipients in the EU separately. With respect to these institutions, the figure includes all loans.
- Cross-jurisdictional claims and liabilities: the data only includes credit institutions' items exceeding the threshold value of 10%.

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There have been no such changes in the structure of the Finnish banking sector after Nordea's redomiciliation as would necessitate adjustment of the threshold of systemic importance. For this reason, it is justified to continue applying the threshold of 2.75% in the identification of O-SIIs.

Based on data as at end-2022, and as in the previous year, Nordea Bank Abp, OP Financial Group and Municipality Finance Plc exceed the threshold of systemic importance (2.75%) and are therefore automatically designated as O-SIIs (Table 2). According to the FIN-FSA's assessment, there are no grounds for designating other credit institutions as O-SIIs.

Nordea Bank Abp is still decidedly the most important credit institution by all O-SII criteria (Table 3). Nordea and OP Financial Group exceed the O-SII threshold in terms of all the four basic criteria, while Municipality Finance exceeds the threshold score in respect of the criteria 'size' and 'interconnectedness'.

Table 2. Finnish credit institutions' O-SII scores as at 31 December 2022

Banking group	O-SII score (%)	O-SII institution
Nordea Bank Abp	64.90	yes
OP Financial Group	11.70	yes
Municipality Finance	4.25	yes
Aktia	0.96	no
Savings Bank Group	0.92	no
S-Bank	0.73	no
Bank of Åland	0.56	no
POP Bank Group	0.44	no
Oma Savings Bank	0.40	no
Danske Mortgage Bank	0.36	no
The Mortgage Society of Finland	0.23	no
Fellow	0.02	no

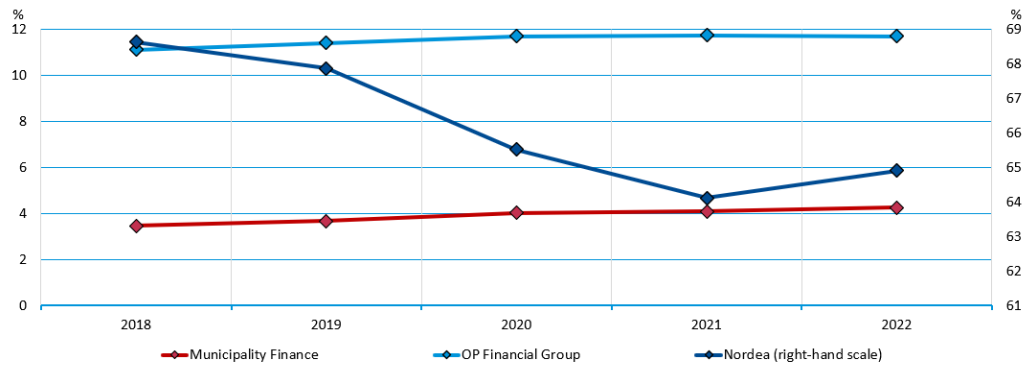
Table 3. Finnish credit institutions' EBA criterion-specific O-SII scores as at 31 December 2022

Banking group	Size	Importance	Complexity	Interconnectedness
Nordea Bank Abp	58.82	47.33	89.28	64.17
OP Financial Group	17.33	16.50	3.29	9.66
Municipality Finance	5.30	1.17	1.90	8.64
Aktia	1.21	1.27	0.20	1.17
Savings Bank Group	1.42	1.54	0.06	0.67
S-Bank	0.99	1.54	0.05	0.31
Bank of Åland	0.66	0.75	0.38	0.44
POP Bank Group	0.64	0.89	0.02	0.22
Oma Savings Bank	0.66	0.67	0.00	0.26
Danske Mortgage Bank	0.47	0.30	0.09	0.60
The Mortgage Society of Finland	0.38	0.33	0.01	0.20
Fellow	0.03	0.06	0.00	0.00

Nordea Bank Abp's O-SII score fell steadily until 2021 but trended upwards in 2022 (Chart 1). At the end of 2022, its O-SII score was about 0.8 percentage points higher

than at the end of 2021. Although Nordea's systemic importance increased in terms of all the four criteria, the higher score was largely attributable to growth in intra-financial system assets and liabilities and in debt securities outstanding. Of the other O-SIIs, the systemic importance of Municipality Finance continued to increase moderately in 2022, while the systemic importance score of OP Financial Group turned slightly downwards.

Chart 1. O-SII scores of Finnish O-SIIs



Source: Financial Supervisory Authority.

3 Principles for setting O-SII buffer requirements for Finnish O-SIIs

Requirements of the Act on Credit Institutions and the minimum O-SII buffer rates

In addition to identifying O-SIIs, the FIN-FSA is, under the Act on Credit Institutions, required to review the buffer requirements of O-SIIs on an annual basis. If the review leads to changes in the O-SII buffer rates, the FIN-FSA shall take a decision on this.

Under the Act on Credit Institutions³, the FIN-FSA is required to allocate each O-SII into one of seven buckets based on their assessed systemic importance. As a rule, the O-SII buffer rate of credit institutions allocated to the lowest bucket (credit institutions other than O-SIIs) is 0% of their total risk exposure amount. The buffer requirements of credit institutions in the other buckets (O-SIIs) increase in increments of 0.5 percentage points, with the O-SII buffer rate of the institutions in the highest (seventh) bucket being 3%, as a rule. O-SII buffers must be met with Common Equity Tier 1 (CET1) capital.

³ The Act on Credit Institutions was revised in 2021 (legislative amendment 233/2021) in accordance with the new Capital Requirements Directive (CRD V), which brought changes to macroprudential buffers, among other things. Consequently, the maximum O-SII buffer rate rose to 3.0% (from 2.0%), and, going forward, the O-SII buffer and the systemic risk buffer are to be applied cumulatively (previously only the higher of the two was effective).

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Table 4. O-SII buckets under the Act on Credit Institutions and associated buffer requirements

Bucket	O-SII buffer rate
1	0%
2	0.5%
3	1.0%
4	1.5%
5	2.0%
6	2.5%
7	3.0%

Under the Act on Credit Institutions, the FIN-FSA is required to apply the following criteria in bucketing O-SIIs and determining their buffer requirements:

1. size of the credit institution, as measured by its total liabilities or balance sheet total or consolidated balance sheet total;
2. liabilities of the credit institution and undertakings within its consolidated supervision to other credit institutions and receivables from other credit institutions as well as other direct interlinkages with the financial system;
3. substitutability of the critical functions of the credit institution and undertakings within its consolidated supervision in the event of an undertaking losing its capacity to continue its operations;
4. extent and significance of cross-border operations of the credit institution and undertakings within its consolidated supervision in Finland and in the European Economic Area.

1.

In practice, the bucketing of Finnish O-SIIs and the calibration of O-SII buffers is based on the systemic importance of O-SIIs, which is primarily assessed using the O-SII scores of the EBA Guidelines. The O-SII buffer calibration is also guided by the floor methodology of the European Central Bank (ECB)⁴. The ECB floor methodology establishes a minimum level for the O-SII buffer requirement of each O-SII – determined by the institution-specific overall O-SII score – against which the buffer rate imposed by the national macroprudential authority is assessed in applying Article 5 of the SSM Regulation⁵. If the national macroprudential authority decides to apply an O-SII buffer rate falling below the minimum level given by the floor methodology, the ECB may set a higher requirement than the one intended by the national authority.

On the basis of the ECB's current floor methodology, Nordea Bank Abp's O-SII buffer requirement should be at least 1.0%, while the revised floor methodology⁶ suggests a minimum buffer rate of 1.5%. For OP Financial Group, the minimum buffer requirement is 0.25% under the current floor methodology, and 0.5% under the revised methodology. For Municipality Finance Plc, the minimum requirement is 0.25% under both methodologies. Taking into account that the Act on Credit

⁴ ECB (2017), [ECB floor methodology for setting the capital buffer for an identified Other Systemically Important Institution \(O-SII\)](#).

⁵ Council Regulation (EU) No 1024/2013.

⁶ The revised floor methodology, which uses more recently calibrated data, is discussed in the [EBA Report](#) submitted to the European Commission in 2020. The entry into force of the new floor methodology was postponed due to the COVID-19 pandemic. The revised methodology was adopted in November 2022 at the meeting of the Macroprudential Forum of the ECB Governing Council and of the Supervisory Board. On 21 December 2022, the Governing Council issued a [statement](#) on the application of the revised floor methodology as of 1 January 2024.

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Institutions requires the application of buffer rate increments of 0.5 percentage points and that a buffer rate of 0% would be contrary to the spirit of the regulations and the ECB floor methodology, it can be considered that, in practice, for OP Financial Group and Municipality Finance, the minimum buffer rate is 0.5%.

2.

FIN-FSA's methodologies for calibrating O-SII buffers

The higher-than-average level of concentration of the Finnish banking sector and the large size of its most significant credit institutions relative to the national economy support the application of O-SII buffer rates above the minimum level given by the ECB's floor methodologies. Buffer requirements that are proportionate to systemic importance, and strong capital adequacy positions, also underpin credit institutions' ability to raise market funding.

The FIN-FSA reviews O-SII buffers by using two alternative bucketing methods in which O-SIIs are allocated to seven buckets on the basis of their assessed systemic importance. In both methods, systemic importance is measured with the O-SII scores calculated in accordance with the EBA Guidelines. In the first method – the linear approach – the O-SII score-based bucket widths are equal, corresponding to the threshold of systemic importance (2.75%). The FIN-FSA has applied a similar method in calibrating O-SII buffers in previous years.

In the second method, the bucket widths are determined on the basis of the equal expected impact (EEI) approach. The method has been applied e.g. in calibrating buffer requirements for global systemically important institutions (G-SIIs).⁷ Under the EEI approach, the buffer requirements of systemically important institutions (SIIs) are calibrated so that the expected social costs from the default of an SII equal those from the default of a non-SII. The parameters of the EEI approach applied by the FIN-FSA are calibrated based on the ECB's analyses⁸. Table 5 illustrates the bucket widths under the linear and the EEI approach and shows the indicative O-SII buffer requirement applicable to each bucket.

Table 5. O-SII buckets and indicative buffer requirements under the linear approach and EEI approach

Bucket	O-SII score (linear approach)	O-SII score (EEI approach)	Indicative O-SII buffer rate
1	0–2.75	0–2.75	0.0%
2	2.75–5.50	2.75–6.00	0.5%
3	5.50–8.25	6.00–10.00	1.0%
4	8.25–11.00	10.00–17.00	1.5%
5	11.00–13.75	17.00–28.00	2.0%
6	13.75–16.50	28.00–48.00	2.5%
7	16.50–	48.00–	3.0%

See Federal Reserve (2015), [Calibrating the GSIB Surcharge](#).

⁸ The calculation uses, as the β parameter in the EEI approach, the median of β parameters estimated, using different approaches, from panel data on risk-weighted assets and losses of euro area banks for 2000–2017. Systemic importance is measured with the O-SII scores calculated as per the EBA Guidelines, and the O-SII threshold is 2.75%. The buffer estimates given by the EEI approach are scaled down to ensure that the O-SII buffers do not exceed the regulatory limits and that the relative differences between the institution-specific buffer estimates do not change.

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Table 6 illustrates Finnish O-SIIs' current O-SII buffer requirements and recommended buffer rates under the two alternative bucketing approaches. The Table also provides the minimum O-SII buffer rates derived from the outcomes of the ECB floor methodologies. The recommended buffer rates under the different calibration approaches suggest that Municipality Finance's current O-SII buffer of 0.5% is proportionate to the institution's systemic importance. OP Financial Group's current O-SII buffer rate corresponds to the one obtained under the EEI approach but using the linear approach the buffer rate could be raised from the current 1.5% to 2.0%. However, OP Financial Group's systemic importance decreased slightly from 2021, which supports maintaining its O-SII buffer at the current level. The Group's O-SII buffer requirement was raised in 2022, from 1.0% to 1.5%, with effect from 1 January 2023.

Nordea Bank Abp's O-SII buffer rate was raised from 2.0% to 2.5% in 2022, effective from 1 January 2023. The buffer results of the different bucketing approaches for Nordea suggest that its O-SII buffer rate could be raised to the regulatory upper limit of 3.0% (bucket 7). This would be supported e.g. by the fact that Nordea is the most significant O-SII in the whole EU both as measured by the O-SII score and relative to the national financial system.⁹ There are also justifications for not setting the highest possible buffer requirement for Nordea and keeping it unchanged at 2.5% (bucket 6). This would provide an incentive for the most significant credit institutions within the buffer framework to avoid increasing their systemic importance.

The banking union can be regarded as reducing the systemic importance of Nordea Bank Abp in particular when examining the different O-SII criteria, as the institution is very large and operates widely in many countries. This would give a justification for the more moderate O-SII buffer requirement for Nordea. The same arguments would also give a justification for keeping the buffer requirements for OP Financial Group and Municipality Finance unchanged.

The first pillar of the banking union – the Single Supervisory Mechanism (SSM) – has improved and harmonised supervisory tools and practices in participating countries and strengthened banks' balance sheets and loss absorbency. This can be considered to have reduced the importance of Nordea as measured by its O-SII criteria 'size', 'interconnectedness' and 'complexity'. The Single Resolution Mechanism (SRM) and close cooperation with the resolution authorities of the other Nordic countries has improved the conditions for effective and harmonised resolution of cross-border banks in times of crises. In assessing credit institutions' systemic importance, this reduces the relevance of cross-jurisdictional claims and liabilities and thereby that of the O-SII criterion 'complexity'. In addition, the minimum requirement for own funds and eligible liabilities (MREL) set for banks in connection with resolution planning reduces the relevance of the O-SII criterion 'importance'. This is because the MREL requirement improves the conditions for effective resolution and promotes the continuity of functions critical for society.¹⁰ Furthermore, crisis preparedness by institutions and authorities reduces the relevance of the criteria 'size' and 'interconnectedness'.

⁹ See the [O-SII-scores](#) published on the EBA website.

¹⁰ Resolution planning seeks to ensure the continuity of critical functions carried out by an institution, such as deposit taking and payment services, in crisis situations. The minimum requirement for own funds and eligible liabilities (MREL) set for banks in connection with resolution planning promote investor responsibility and improve the resolvability of institutions and the conditions for the application of resolution measures.

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Table 6. Indicative buffer requirements for Finnish O-SIIs under different approaches

Banking group	Current O-SII buffer rate	Indicative O-SII buffer rate (linear approach)	Indicative O-SII buffer rate (EEI approach)	Minimum O-SII buffer rate, ECB floor methodology
Nordea Bank Abp	2.5%	3.0%	3.0%	1.0% / 1.5%
OP Financial Group	1.5%	2.0%	1.5%	0.5%
Municipality Finance Plc	0.5%	0.5%	0.5%	0.5%

Hence, single banking supervision and crisis resolution reduce the probability of failures and distress of systemically important banks operating within the banking union, thereby lowering the related costs to society. This supports the more moderate levels for O-SII buffer requirements.

Conclusions

Based on the O-SII scores as at end-2022, the credit institutions designated as O-SIIs in Finland are Nordea Bank Abp, OP Financial Group and Municipality Finance Plc, as in the previous years. Considering the recommended buffer requirements under the different calibration methodologies and the reasons stated above, the FIN-FSA finds it justified to maintain the O-SII buffers of all the three O-SIIs at their current levels: 2.5% for Nordea, 1.5% for OP Financial Group and 0.5% for Municipality Finance. The systemic importance of Finnish O-SIIs has not changed significantly during the year, and therefore the O-SII buffer requirements reviewed in June 2022 can be regarded as proportionate to the systemic risks related to the systemic importance of O-SIIs.

Table 7. Finnish O-SIIs' buffer requirements and O-SII buckets

Banking group	O-SII buffer rate (current buffer rate)	O-SII bucket under the Act on Credit Institutions
Nordea Bank Abp	2.5% (2.5%)	6
OP Financial Group Plc	1.5% (1.5%)	4
Municipality Finance	0.5% (0.5%)	2

Higher risks in the financial markets, rapid inflation, interest rate increases and the prolongation of the war in Ukraine have fuelled financial market uncertainty and concerns over financial stability. Slower economic activity in Finland and uncertainty about future economic forecasts have weakened the operating environment for the financial sector. The banking sector's credit risks have also increased. Higher energy prices, living costs and interest rates are eroding borrowers' ability to service their debts. Risks in the real estate market have increased and house prices have turned downwards. There is a risk of higher credit losses if collateral values decline and

borrowers run into payment difficulties. The recent turbulence in the international financial markets may also constrain access to funding for banks, thereby weakening their lending capacity.

The higher risks and uncertainties in the financial markets further emphasise the necessity of macroprudential buffers and their appropriate calibration. The banking sector's strong capital adequacy position provides protection against losses caused by severe shocks to the economy or the financial system and improves the availability and terms of market-based funding.