



Reforms in the Icelandic Financial Sector

Undertaken since October 2008

Since the collapse of the Icelandic banking system in October 2008, Iceland has carried forward wide-ranging and systemic reforms of the financial sector. This has been done in accordance with international best practise with the clear aim of building up a solid and sustainable financial system.

- In November 2008, as part of its Stand-By Arrangement with the International Monetary Fund (IMF), the Icelandic government requested an experienced bank supervisor to assess the regulatory framework and supervisory practices in Iceland and to propose needed changes. The expert, Mr. Kaarlo Jännäri, a former chairman of the Finnish FSA, was asked to assess the framework of rules on liquidity management, connected lending, large exposures, cross-ownership, and the “fit and proper” status of owners and managers.
 - His main conclusion was that the Icelandic legal framework was comparable to that of other EEA states, pointing out the necessity of making the legislation more precise and stringent in several areas. A committee appointed by the Minister of Economic Affairs to review the legislative framework was established, mandated to draft new legislation.
 - The committee as well as the Ministry have followed closely the work being done within the EU in the financial sector especially as regards the work of the committee in the field of supervision. The committee delivered its interim proposals to the Minister of Economic Affairs last November and a legislative proposal was put before the parliament of Iceland on 29 January 2010.
- ### A New Bill on the Financial Market
- The Financial Supervisory Authority (FME) is given increased discretionary powers.
 - The role and responsibility of internal auditing and risk management is increased. The tenure of external auditors is limited to 5 years.
 - A credit registry, containing data on all borrowers above a certain limit, is established. Borrowers not subject to official supervision will have a legal duty to disclose their total borrowings to the FME.
 - Provisions on the conduct of financial undertakings will be enhanced and the role of the dispute resolution committee of the financial market increased.
 - Tightened permits for financial undertakings to acquire or hold own shares either directly or through subsidiary entities.
 - No lending against collateral in own shares.
 - Stricter rules on lending to members of the board of directors, CEOs and key personnel.
 - Stricter rules on the effects of lending against collateral in the shares of other financial undertakings on equity (capital ratios).
 - More detailed rules on large exposures.
 - Increased possibilities of the FME to oppose acquisitions of qualified holdings.

- Increased responsibilities of the members of the board of directors.
- Stricter rules on dealings with own staff of financial undertakings.
- Rules on remuneration, bonus systems and severance agreements established.
- The provision extends the authorization provided to the FME when the Transparency Directive was implemented and now has a general reference in the work of the FME.

The Central Bank's Governance has been changed

A New Ministry of Economic Affairs

- is administratively responsible both for the Financial Supervision Authority and the Central Bank, thereby increasing its possibility to enhance macro prudential supervision.

The FME is Investigating Various Cases

- of possible wrongdoings in the financial sector. The FME has by December 2009 forwarded 31 cases to the Special Prosecutor, established to investigate possible wrongdoings in the lead-up to the crisis.
- The FME will place emphasis in its annual work plan on higher on-site inspection frequency, by means of more specialization within the authority and more resources allocated to on-site inspection.
- To bolster FME investigative capacity, the FME has already established a forensic accounting unit with a specialized staff to uncover and prevent financial fraud and wrongdoing and play a proactive role in risk reduction. The unit will also support prosecuting efforts.
- As part of the Emergency Act in October 2008, the FME was given extended powers to intervene in operations of ailing financial undertakings as well as an extended role in the restructuring of the banking system.
- In March 2009, a bill of law was passed by the parliament allowing the FME to make public all its decisions, the objective being to amplify transparency in the work of the FME.
- with one governor and a deputy governor appointed through a rigorous process. A Monetary Policy Committee has been appointed with 2 external academics. The bank's independence has thus been strengthened further.
- A draft bill of law for a new Act on Deposit Guarantees and Investor Compensation is being discussed in the parliament. The objective of the bill is to implement the EU directive of March 2009 as well as making amendments necessary in light of the crisis.
- A draft bill of law amending the Act on UCITS is in parliamentary proceedings. The Act is being amended in light of the financial crisis and to implement the latest EU acquis on the subject.
- The Minister of Economic Affairs has put forward to the parliament a bill of law which introduces amendments to the Act on Limited Liability Companies and the Act on Private Limited Liability Companies. The bill proposes amendments as regards ownership, executive chairman and gender ratios within boards, management and among employees of companies. The objective of the bill is to introduce more transparency into corporate ownership and voting structures, gender equity with respect to governing boards and employees and that the chairman of the board will not work for the company in another capacity than as chairman.

Iceland, with a population of around 317,000, is a constitutional republic with a parliamentary government. Iceland joined the United Nations in 1946, became a founding member of the OECD in 1948, of NATO in 1949 and joined EFTA in 1970. With Iceland's accession to the European Economic Area in 1994, Iceland gained access to EU's internal market. The foundations of the Icelandic economy, with a GDP of \$11.4 billion (IMF 2009 est.) are fisheries, industry, tourism, pharmaceuticals and services.