Banc Ceannais na hÉireann
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Identification of Other Systemically Important Institutions in Ireland and Announcement of Associated Buffers

2016 review of the O-SII framework

Under Regulation 121(1) of the European Union (Capital Requirements) Regulations 2014 (S.I. No. 158 of 2014) ("CRD Regulations"), the Central Bank of Ireland ("Central Bank") is designated as the authority in charge of identifying other systemically important institutions ("O-SII") which have been authorised within the State. Under Regulation 123(2) of the CRD Regulations, the Central Bank may require each O-SII to maintain an O-SII buffer of up to 2 per cent of the total risk exposure amount calculated in accordance with Article 92(3) of the Capital Requirements Regulation (EU) No 575/2013[1].

O-SIIs are institutions which are systemically important to the domestic economy or to the economy of the European Union (EU). The objective of the O-SII buffer is to reduce the probability, and potential impact, of these institutions' failure on the domestic economy. Under the CRD Regulations, the Central Bank must review on an annual basis the identification of O-SIIs and the appropriate O-SII buffer rates for each individual O-SII identified.

The O-SII framework was introduced in Ireland in 2015 when two institutions, namely Allied Irish Banks plc and The Governor and Company of the Bank of Ireland, were identified as systemically important, with a buffer of 1.5 per cent phased-in between 1 July 2019 and 1 July 2021.

Following the 2016 review of the O-SII framework, seven institutions are identified as systemically important in Ireland and buffer rates have been applied to these institutions. The increase in the numbers of institutions identified as systemically important in 2016 versus 2015 reflects that the Central Bank, in aligning with other National Competent Authorities ("NCAs"), and thereby ensuring consistency and harmonisation between each NCA, has fully followed the EBA Guidelines. The list of O-SIIs, O-SII buffers[2] and associated phase-in periods are laid out in Table 1.

As a member of the Single Supervisory Mechanism (SSM), decisions relating to the application of the O-SII buffers are also made in conjunction with the European Central Bank (ECB) and are without prejudice to any powers of the ECB under the SSM Regulations[3] with respect to O-SII buffer settings.

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[1] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.
[2] To be held in the form of CET1.
[3] See Council Regulation (EU) No 1024/2013 ('SSMR'), Regulation (EU) No 468/2014 of the ECB ('SSMFR') and the CRD Regulations.

Table 1: 2016 O-SII and associated phased-in buffer requirements

O-SII	Level of consolidation	O-SII Buffer		
		1 July 2019	1 July 2020	1 July 2021
Allied Irish Banks plc (AIB)	Consolidated	0.5%	1.0%	1.5%
The Governor and Company of the Bank of Ireland (BOI)	Consolidated	0.5%	1.0%	1.5%
Permanent tsb Group Holdings plc (ptsb)	Consolidated	0.25%	0.5%	0.5%
Ulster Bank Ireland Designated Activity Company (Ulster)	Individual	0.25%	0.5%	0.5%
Citibank Holdings Ireland Ltd (Citigroup)	Consolidated	0.25%	0.5%	0.5%
UniCredit Bank Ireland plc (UniCredit)	Individual	0.25%	0.25%	0.25%
DePfa Bank plc (Depfa)	Consolidated	0.0%	0.0%	0.0%

Identification of O-SIIs

Regulation 122 of the CRD Regulations outlines that O-SIIs should be identified on the basis of at least any of the following criteria*: size, importance for the economy of the Union or the State, significance of cross-border activities, interconnectedness of the institution or group with the financial system*. The European Banking Authority (EBA) has issued Guidelines on criteria to assess O-SIIs (EBA/GL/2014/10) ("EBA Guidelines"),[4] with a view to further harmonising identification practices across the EU. The EBA Guidelines establish a scoring process for assessing the systemic importance of an institution based on indicators relating to size, importance, complexity/cross-border activity, and interconnectedness.

Taking account of these considerations, the Central Bank calculated a score for each Irish-authorised entity at the highest consolidated level of the part of the group that falls under the remit of the Central Bank. A 350 basis points threshold of systemic importance was used to identify the O-SIIs. This is the standard threshold set out in the EBA Guidelines. Institutions with relative total assets below 0.02 per cent were excluded from the identification process. All institutions identified by the mandatory scoring process in the EBA Guidelines were identified as O-SIIs; no additional institutions were identified. The resultant list of O-SIIs and the EBA score are outlined in Table 2.

[4] https://www.eba.europa.eu/documents/10180/930752/EBA-GL-2014-10+(Guidelines+on+O-SIIs+Assessment).pdf

Table 2: List of O-SIIs for 2016 and EBA scores

O-SII	Overall Score
BOI	2213
AIB	1630
Depfa	920
Ulster	539
UniCredit	510
Citigroup	414
ptsb	385

A separate assessment was carried out for investment firms in scope of the CRD Regulations and which deal on own account or underwrite on a firm commitment basis. The analysis has been completed in accordance with the EBA Guidelines using indicators appropriate for investment firms. This assessment led to no investment firms being identified as O-SIIs for 2017.

Calibration of O-SII buffers

The rationale for the O-SII buffer arises from the negative externalities created by systemically important institutions to the domestic/ European economy, which are not borne fully by the equity and debt holders of these institutions. Higher capital requirements for these institutions can reduce the probability, and impact, of their failure relative to non-systemic institutions, which should neutralise the greater impact the failure of an O-SII would have on the financial system and economy.

The Central Bank's approach to calibrating the O-SII buffers took into account the high level principles of the Basel Committee on Banking Supervision (BCBS) framework[5], the requirements of the CRD Regulations and the specificities of the Irish economy. The approach assessed the systemic importance of each institution after which institutions were grouped and ranked before O-SII buffers were applied. A peer comparison with European institutions was then conducted.

Assessing systemic importance:

When assessing the systemic importance of supervised institutions in Ireland, the mandatory requirements laid out in Regulation 122 of the CRD Regulations and the EBA Guidelines were used. The EBA Guidelines identify a mix of banks as O-SIIs for Ireland. Given the wide variation in business models operating in Ireland, it was important to also consider the business model of the individual institutions and how this affected the EBA scores. Each institution's sub-score was examined to provide a clearer picture of the drivers of their high systemic importance score.

[5] BCBS (2012), "A framework for dealing with domestic systemically important banks", Basel Committee on Banking Supervision, October 2012 http://www.bis.org/publ/bcbs233.pdf

Grouping and ranking institutions:

Extensive analysis was then carried out using the Expected Impact Framework [6]. This method aims to equalise the expected impact of each O-SII with that of a reference non-O-SII. Two main variables were calculated: the probability of default (PD) as a function of capital and the relative economic cost of failure (ECF). Historical bank losses were used to calculate the PD of an Irish institution as a function of capital and a number of approaches were taken to measuring ECF of an institution including; total EBA score; EBA importance sub-score and average market share in Irish loans and deposits. The resultant analysis provided the following observations:

- Under all assumptions, BOI and AIB receive significantly higher buffers than other institutions.
- When measures of cost of failure with greater focus on the real economy are used, such as share of domestic loans and deposits, implied buffers for domestically-focussed institutions increase.
- When measures of cost of failure with greater focus on the Irish economy are used, the international institutions are less systemically important.

Considering these observations with the assessment of systemic importance, institutions were placed into one of the below groups:

Table 3: Groups for O-SII process

	Group description	O-SIIs
Group 1	Highly systemically important domestic banks	BOI and AIB
Group 2	Systemically important domestic banks	Ulster and ptsb
Group 3	Large international banks	Citigroup
Group 4	Smaller international banks	UniCredit
Group 5	Banks which are in run-off	Depfa

Applying buffer rates:

Buffer rates were then assigned to each group. The maximum buffer of 2 per cent is not yet assigned to any institution as a disincentive for banks to grow larger and attract this higher buffer rate. The buffer rate was set taking into account the analysis of the nature and degree of an institution's systemic importance, the range of buffer rates implied by the results of the expected impact analysis, a peer review of buffer rates set by other authorities for similar institutions and both the BCBS and EU frameworks.

At a European level few countries have set 0 per cent O-SII buffers, however it was decided to do so in the case of Depfa due to the very specific circumstances of this institution. The institution is

[6] For more information see "Calibrating the GSIB Surcharge" Federal Reserve Board (2015) or "The FPC's framework for the systemic risk buffer" Bank of England (2016).

currently in run-down and has not written new business since September 2008. The on-going strategy is to wind down its portfolios (through a process of asset maturity and the transfer of a portion of longer termed assets to its parent) in a manner that maintains shareholder value.

Peer comparison:

The Central Bank observed other European banks where G-SII, O-SII and systemic risk buffers have been set and compared the size of the buffer to the size of the bank relative to the national economy. It was clear that a great deal of heterogeneity exists in the setting of a buffer rate. When considering an O-SII buffer of 1.5 per cent for AIB and BOI, it appears to be in line with European peers given assets to GDP levels however it is noted that there is a large dispersion among country buffer rates.

Phase-in period

In establishing the phase-in period, the 2019 start date was guided by the end of the phase-in for other capital buffers under the CRD Regulations, whilst the gradual phase-in reflected the trade-off between allowing the banks to continue to recover and to support Irish economic growth and requiring them to build adequate buffers to ensure resilience and financial stability. For banks which do not provide credit to the domestic market, it has been decided to introduce the buffers at the same time, 1 July 2019, for consistency purposes. The phase-in period for these banks varies, depending on the buffer rate set.