

# Íslandsbanki's Corporate Governance Statement for 2016

# Corporate Governance Statement 2016

The Board of Directors of Íslandsbanki is committed to excellence in corporate governance complying with the applicable regulatory standards and best international practices in the field of corporate governance.

Íslandsbanki's governance practises are consistent with general corporate governance guidelines for entities regulated by official supervisors and regulatory instruments. The regulatory framework for corporate governance practices within Íslandsbanki consists of the law applicable to entities subject to the supervision of the Financial Supervisory Authority (FME) as well as other applicable law and regulations, including those imposed by the FME and Nasdaq Iceland, available at their respective websites ([www.fme.is](http://www.fme.is) and [www.nasdaqomxnordic.com](http://www.nasdaqomxnordic.com)). The applicable law includes, inter alia, the Act on Financial Undertakings no. 161/2002, the Act on Securities Transactions no. 108/2007, the Act on Competition no. 44/2005 and the Act on Public Limited Companies no. 2/1995, which along with the Íslandsbanki's Articles of Association lay the foundation for the Bank's existence and activities. The relevant law is available on the Icelandic legislature's website ([www.althingi.is](http://www.althingi.is)).

## Exemplary in Corporate Governance

Íslandsbanki is committed to maintaining high standards of governance complying with best governance practices. Íslandsbanki was first recognized as "Exemplary in Corporate Governance" in March 2014 by the Center of Corporate Governance at the Institute for Business Research, University of Iceland. The recognition was awarded following a comprehensive review of the practices of the Board, Board subcommittees and management. The recognition was renewed in March 2015 and 2016 and again in February 2017.

Íslandsbanki maintains a Good Governance Policy, the Decision Making Matrix, which outlines all major decisions the Bank may wish to take under given circumstances. The policy is a part of the Bank's effort to improve its material actions and enhance stakeholders' trust. The Decision Making Matrix sets specific conditions to all major decision-making. Furthermore, it sets the requirement that all such decisions are taken after consultation with the relevant parties within the Bank and on the basis of the best information available at the time.

## Compliance with Corporate Governance Guidelines

In accordance with Paragraph 7 of Article 54 of the Act on Financial Undertakings no. 161/2002, the Bank is required to comply with accepted guidelines on the governance of financial undertakings. The Board of Directors follows the Corporate Governance Guidelines (5th ed.) issued by the Iceland Chamber of Commerce, Nasdaq Iceland and SA-Business Iceland (hereinafter the Guidelines). The Guidelines are available on [www.corporategovernance.is](http://www.corporategovernance.is). Governance practices of the Bank are consistent with the Guidelines. Íslandsbanki complies with them in all respects except for certain items in Articles 1.5 and 2.9. The following discussion explains the reasons behind these exceptions as well as measures taken in relation to them.

In accordance with Article 1.5 of the Guidelines the shareholders' meeting shall appoint members to a nomination committee or decide how they should be appointed. The Bank's shareholders, as well as the Board, have not deemed it necessary to appoint a nomination committee at this time given the ownership of the Bank. Candidates for board membership are nominated by the Icelandic Government, sole owner of the Bank, through a selection process administered by Icelandic State Financial Investments (ISFI) in accordance with article 7 of the Act no. 88/2009 on the Icelandic State Financial Investments (ISFI Act).

According to Article 2.9 of the Guidelines it is preferred that the Board sets a policy of social responsibility and a code of ethics. The Executive Board of the Bank adopted a code of conduct for the Bank in January 2011, which all employees were involved in formulating. The Board will be adopting a new code of ethics in the year 2017.

## Main aspects of Risk Management and Internal Control

### Internal Control

The risk management and internal control framework of the Bank is based on the three-lines-of-defence model, as referred to in the European Banking Authority's Guidelines on Internal Governance, and aims for informed decision-making and strong risk awareness throughout the Bank. The framework is intended to ensure effective and efficient operations, adequate control of risks, prudent conduct of business, reliability of financial and non-financial information reported internally and externally, and compliance with laws, regulations, supervisory requirements and the Bank's internal rules.

The first line of defence consists of the Bank's business and support units; the second line of defence is comprised of the Bank's internal control units, Risk Management and Compliance; and the third line of defence is Internal Audit which keeps the Board and management informed of the quality of corporate governance, risk management and internal controls, including by performing independent and objective audits.

### Risk Management

The Board of Directors has a supervising role monitoring the execution of set policies, the sound control of accounting and financial management and ensures that group internal audit, compliance and risk management are effective at all times.

The management committees: The Executive Board; Risk Committee; Asset and Liability Committee; and Investment Committee, are responsible for implementing risk management practises and internal monitoring in accordance with Board authorisation. Under this authorisation, these committees issue detailed guidelines for risk assessment and individual risk thresholds in accordance with the Bank's defined risk appetite.

## Corporate Governance Statement 2016

Further information on the Bank's risk management structure and internal control can be found in the Bank's annual Pillar 3 Report which is published on the Bank's website.

### Audit and accounting

The CEO ensures that Directors of the Board are provided with accurate information on the Bank's finances, development and operations on a regular basis.

The Bank's Finance division is responsible for the preparation of the Bank's consolidated financial statements in line with the International Financial Reporting Standards (IFRS). The Board's Audit Committee gives its opinion on annual and interim consolidated financial statements before their submission for Board approval and endorsement. Management reporting is generally presented to the Board 10 times a year. The external auditors review and audit annual consolidated financial statements. An evaluation of weaknesses in the Bank's internal controls in relation to the accounting process is included in the external auditors report to the Board's Audit Committee.

The consolidated financial statements are published on an annual and quarterly basis. The Risk management notes to the consolidated financial statements form part of the accounting process, see further notes 58-83 of the consolidated financial statements.

As is provided for in the Act on Financial Undertakings and the Bank's Articles of Association, the Bank's external audit firm is elected at the AGM for a term of five years. At the 2016 AGM the Icelandic National Audit Office (INAO) was elected to serve as Íslandsbanki's independent external auditing firm, in accordance with Article 6(2) of Act no. 86/1997 on the Icelandic National Audit Office. The INAO has concluded an agreement and trusting Ernst & Young ehf. with carrying out the Bank's external audit on its behalf.

### Group Internal Audit

Group Internal Audit operates independently from other departments in accordance with Article 16 of the Act on Financial Undertakings no. 161/2002. The department provides Íslandsbanki with independent, objective, assurance over the effectiveness of risk management, control and governance processes. The Chief Audit Executive is engaged by the Board and is responsible for internal audit on a group basis.

### Compliance Officer

As a financial undertaking licensed to conduct securities trading and an issuer of listed financial instruments, Íslandsbanki operates a compliance department. The Bank's Compliance Officer is engaged by the CEO, subject to Board confirmation, conferring the department's mandate. The Compliance officer maintains an independent position within the Bank's organisation and is responsible for monitoring and assessing regularly whether the Bank's operations, regarding securities transactions, are in compliance with applicable law. Furthermore, the Compliance Officer is responsible for assessing and monitoring the Bank's compliance with Act on Measures against Money Laundering and Terrorist Financing no. 64/2006 and he is also the Bank's responsible officer under the US Foreign Account Tax Compliance Act (FATCA) and the OECD Common Reporting Standard (CRS). Moreover, the Compliance Officer oversees compliance risk within the Bank.

## Íslandsbanki Values, Code of Conduct and Social Responsibility

Íslandsbanki's values are the pillars of the Bank's corporate culture, shaping the conduct and attitudes of its employees. The values insist on employees being professional, disciplined in their working procedures, and following matters through – professional, positive and progressive.

In order to maintain and strengthen the credibility and the reputation of the Bank, all employees were involved in formulating the Bank's Code of Conduct which is available on the Bank's website. The aim of the code is to promote good operational and business practices, increase trust and guide employees in their daily work.

Íslandsbanki seeks to work in harmony with the communities in which it operates, delivering support for its immediate environment in the areas of culture, sports, community affairs as well as entrepreneurship and innovation. This participation in community programmes rests on Íslandsbanki's Corporate Social Responsibility Strategy which is set by the Board. The strategy covers five key areas: business, education, environment, human capital, and society. Furthermore, the Bank produces an annual report, Íslandsbanki in the Community: Global Compact, which can be accessed on the Bank's website. For the last eight years Íslandsbanki has been a signatory to the UN Global Compact on social responsibility. The compact is a guide for companies on how to be socially responsible in practice.

## Board of Directors

The Board of Directors comprises seven non-executive directors, and two alternates, elected at each AGM for a term of one year. The Chairman of the Board is elected by the shareholders' meeting. There are no limitations on duration of Board membership.

The Board undertakes the Bank's affairs in between shareholders' meetings unless otherwise provided by law or the Bank's Articles of Association. The Board is responsible for setting the Bank's general strategy and instructs the CEO on its further implementation and execution. The Board has a supervisory role in that it oversees that the Bank's organisation and activities are at all times in accordance with the relevant law, regulations and good business practices. The CEO and Chief Audit Executive are engaged by the Board.

## Corporate Governance Statement 2016

The Rules of Procedure of the Board are adopted in accordance with Article 70 of the Act on Public Limited Companies no. 2/1995 and Article 54 of the Act on Financial Undertakings no. 161/2002. The Board's current rules of Procedure, adopted on 12 January 2017, are available on the Bank's website. According to its Rules of Procedure, at meetings of the Board the presence of at least five members of the Board is required to constitute a quorum. The Board met 19 times in 2016, each time constituting a quorum.

Candidates for board membership are nominated through a selection process administered by ISFI in accordance with Article 7 of the ISFI Act. The Articles of Association of the Bank provide that the ratio of each gender on the Board of Directors shall not be lower than 40%, currently the Board is comprised of four women and three men. In other respects than the foregoing the Board has not set a specific policy on Board diversity.











The Board appoints subcommittees, each one comprising Board members and operating under the terms of a mandate letter from the Board as well as the Rules of Procedure of the Board. The mandate letters of Board subcommittees are available on the Bank's website.



**The Board Audit Committee**, comprising three Board members, assists the Board in fulfilling its oversight responsibilities concerning the financial reporting process, the system of internal control, the audit process and the Bank's process for monitoring compliance with the relevant laws and regulations and its code of conduct. The committee met 10 times in 2016, each time constituting a quorum.

**The Board Risk Management Committee**, comprising four Board members, is responsible for assisting the Board in providing oversight of senior management's activities in managing risk relevant to the Bank's operations. This includes credit risk, market risk, operational risk, liquidity risk, compliance risk and reputational risk. The committee met 10 times in 2016, each time constituting a quorum.

**The Board Corporate Governance, Compensation and Human Resource Committee**, comprising three Board members, assists the Board in overseeing the development and the regular assessment of the Bank's approach to corporate governance issues and board effectiveness. Furthermore it is responsible for providing oversight regarding compensation and human resource issues. The committee met 7 times in 2016, each time constituting a quorum.

Structure and composition of Board subcommittees is as follows:

	The Board Corporate Governance, Compensation and HR Committee	The Board Audit Committee	The Board Risk Management Committee
Fridrik Sophusson			
Anna Thórdardóttir			
Audur Finnbogadóttir			
Árni Stefánsson			
Hallgrímur Snorrason			
Heidrún Jónsdóttir			
Helga Valfells			

 Member
  Chair

### Members of the Board

**Fridrik Sophusson**, chairman of the Board, born in 1943, joined the Board in January 2010. He has comprehensive experience in fiscal policy-making, management, and public service in Iceland. He has also served as a board member in several companies and institutions. He was Managing Director of the Icelandic Management Association from 1972 until 1978, when he was elected to Parliament. During his tenure as an MP, he held the position of Minister of Industry and Energy in 1987-1988 and Minister of Finance in 1991-1998. Fridrik was appointed CEO of Landsvirkjun, the National Power Company of Iceland, in 1999 and held that position for almost 11 years. He serves as chairman of the board of Hlíðarendi ses. as well as as an alternate board member of Fondament ehf. Fridrik holds a Cand. Jur. degree in Law from the University of Iceland.

Sub-Committees: Chairman of the Board Corporate Governance, Compensation and Human Resource Committee.

## Corporate Governance Statement 2016

**Anna Thórdardóttir**, born in 1960, joined the Board in April 2016. She has been a board member of a number of companies and other entities, including KPMG and the institute of State Authorised Public Accountants in Iceland. She is currently a member of the board of the Icelandic Center for Future Studies (Framtíðarsetur Íslands) and the Chairman of the Board Audit Committee of Hagar hf. Anna was an employee of KPMG in 1988-2015 and a partner from 2009, and was responsible for the audit of the following companies: Reitir, Hagar, 365, Baugur Group, Vodafone, Landfestar, Landey, 10-11, and Félagsbústadir. Anna holds a Cand. Oecon. degree in Business Administration from the University of Iceland and she is a Chartered Accountant. She studied for Cand. Merc degree in Finance and Accounting at Handelshøjskolen in Århus, Denmark.

Sub-Committees: Chairman of the Board Audit Committee and a member of the Board Risk Management Committee.

**Audur Finnbogadóttir**, born in 1967, joined the Board in April 2016. She has extensive experience in the field of financial markets. She was Managing Director of Lífsverk pension fund, the pension fund for employees for the municipality of Kópavogur, and MP bank. She has held the position of Chairman of the Board of the Competition Authority in Iceland and been a member of the board of the Iceland Enterprise Investment Fund, Icelandair Group, Landsnet, Nordlenska and New Kaupthing Bank. Audur is currently a member of the board of Rotaryklúbbur Rvík-Austurbær. Audur holds a B.Sc. degree in International Business from the University of Colorado and an MBA from Reykjavík University. She is a securities broker licensed by the Icelandic Ministry of Finance and Economic Affairs.

Sub-Committees: Member of the Board Risk Management Committee.

**Árni Stefánsson**, born in 1966, joined the Board in April 2016. He has extensive management experience in energy and heavy industries in Iceland. He is currently manager and member of the executive board at the primary aluminium plant Rio Tinto Alcan - ISAL. He was previously a manager and member of the executive board of Century Aluminium plant Nordurál in Grundartangi, a manager and vice-president of the Icelandic electric transmission grid company Landsnet, and a manager with Landsvirkjun, the National Power Company of Iceland. Árni holds an M.Sc. degree and B.Sc. degree in electrical engineering from Alborg University in Denmark.

Sub-Committees: Member of the Board Risk Management Committee.

**Hallgrímur Snorrason**, born in 1947, joined the Board in April 2016. He is an independent consultant in official statistics. He was Director of Statistics Iceland in 1985-2007 and Deputy Managing Director of the National Economic Institute of Iceland in 1980-1984. Has been a member of the board of several companies, including Útvegsbanki Íslands, Skýrr and Audur Capital. He has also chaired a number of governmental committees, both domestically and in relation to cooperation with the Nordic region, EFTA, the EU and the OECD. Hallgrímur holds an M.Sc. degree in Economics from Lund University in Sweden and a B.Sc. degree in Economics from the University of Edinburgh.

Sub-Committees: Member of the Board Corporate Governance, Compensation and Human Resource Committee and the Board Audit Committee.

**Heiðrún Jónsdóttir**, born in 1969, joined the Board in April 2016. She is an attorney at law with Fjeldsted and Blöndal Legal Services. Previously she served as the Managing Director of Legal and Human Resources at Eimskipafélag Íslands, Managing Director at Lex Legal Services, and Managing Director of Legal and Human Resources at KEA. She has extensive experience serving as a board member since 1998. She has been a Chairman of the Board of Directors at Nordlenska, Íslensk Verðbréf, and Gildi pension fund and has been a member of the board of Ollúverslun Íslands, Síminn, Reiknistofa bankanna, Ístak, the Icelandic Pension Funds Association, Silicor Materials Iceland, and Gildi pension fund. Heiðrún holds a Cand. Jur degree from the University of Iceland and is a securities broker licensed by the Icelandic Ministry of Finance and Economic Affairs. In 2016-2017, she is attending AMP, the Advanced Management Program at IESE Business School in Barcelona.

Sub-Committees: Member of the Board Corporate Governance, Compensation and Human Resource Committee and the Board Audit Committee.

**Helga Valfells**, born in 1964, joined the Board in September 2013. Most recently she was the Managing Director of NSA Ventures, an Icelandic venture capital fund. Previous employers include Estée Lauder UK, Merrill Lynch Europe, and the Trade Council of Iceland. As an entrepreneur she has participated in founding start-up companies as well as acting as an advisor to the Icelandic Minister of Business Affairs. Furthermore, she has worked as an independent consultant for a number of export companies from Iceland, the UK, and Canada. She serves as Chairman of the Board of Frumtak GP ehf. and is a member of the boards of Alþjóðaskólinn á Íslandi ehf., Klak Innovit ehf., Mentor ehf., Transmit ehf., Dohop ehf. and Vesturgardur ehf. She is an alternate board member of Akthelia ehf., Azazo hf., FSÍ (Framtakssjóður Ísl) slhf., Greencloud ehf., InfoMentor ehf., Íslensk Nýsköpun ehf. and Norrænar Myndir ehf. Helga holds a B.A. degree in Economics and English Literature from Harvard University and an MBA from London Business School.

Sub-Committees: Chairman of the Board Risk Management Committee.

Alternate members of the Board are two; **Herdís Gunnarsdóttir** and **Pálmi Kristinsson**, both since April 2016.

All members of the Board are considered independent from the Bank, its main clients, competitors and shareholder.

# Corporate Governance Statement 2016

## Board Performance Assessment

At least once a year, as provided for in the Board's Rules of Procedure, the Board assesses its work, procedures and practices as well as each of its members. This performance assessment is intended to improve working methods and increase the efficiency of the Board. The assessment entails an evaluation of the strengths and weaknesses of the Board's work and practices. This is i.a. based on Board members' self-assessment on whether the Board rules of procedure have been complied with in all respects, a status taken of the specific priorities set by the Board regarding risk management and internal control within the Bank as well as a follow up on how certain decisions of the Board have been implemented.

## Executive Management

The Chief Executive Officer (CEO) is responsible for the day-to-day operations of the Bank pursuant to set policies and resolutions of the Board. The CEO is also required to ensure that the Bank's operations are in compliance with applicable law and the Bank's Articles of Association at all times. The CEO engages the Bank's Compliance Officer and appoints members of the Executive Board and other management committees.

**Birna Einarsdóttir**, born in 1961, is the CEO of Íslandsbanki. She holds a Cand. Oecon. degree in Business Administration from the University of Iceland and an MBA degree from the University of Edinburgh. Birna has been with Íslandsbanki and its predecessors in various divisions for 22 years and CEO since 15 October 2008. Previous to that she was a senior product manager at the Royal Bank of Scotland and Marketing Manager for the Icelandic Broadcasting Company Stöð 2 (Channel 2) and Íslensk Getspá. Birna is the Chairman of the Board of Icelandic Financial Services Association and is a member of the board of SA-Business Iceland. Birna is considered independent from the Bank, its main clients, competitors and shareholder.

Together with the CEO, the Executive Board manages the daily activities of the Bank according to the strategy set out by the Board. It consists of nine people, including the CEO: Birna Einarsdóttir, CEO since October 2008, Björgvin Ingi Ólafsson, Managing Director of Relationship Banking since October 2014, Elín Jónsdóttir, Managing Director of Wealth Management since July 2014, Jón Gudni Ómarsson, Chief Financial Officer since October 2011, Sigríður Olgeirsdóttir, Chief Operating Officer since September 2010, Sverrir Örn Thorvaldsson, Chief Risk Officer since November 2010, Tryggvi Björn Davíðsson, Managing Director of Markets since September 2011, Una Steinsdóttir, Managing Director of Retail Banking since October 2008 and Vilhelm Már Thorsteinsson Managing Director of Corporate Banking since October 2008.

The CEO and management committees are responsible for implementing risk management practices and internal monitoring in accordance with Board authorisation. The committees are appointed by the CEO, and their letters of mandate and rules of procedure approved by the Board.

The Executive Board is responsible for the Bank's operational risk management framework and supervises legal risk, reputational risk, business risk and strategic risk as well as the Bank's formal product approval policy.

The Risk Committee manages and supervises credit related matters and other counterparty risk, in accordance with the Bank's credit policy and lending rules.

The Asset and Liability Committee monitors other financial risks, such as market risk, liquidity risk, and interest rate risk in the Bank's non-trading portfolio.

The Investment Committee makes decisions on the purchase or sale of equity holdings in companies, as well as other types of investments, including investment funds and real estate.

Further to the above Human Resources, the Legal and Compliance departments report directly to the CEO.

## Arrangement of communications between shareholders and the Board

The Board communicates with shareholders in accordance with the relevant laws, the Bank's Articles of Association and the Board's Rules of Procedure. Members of the Board of Directors shall, in their duties and decision-making, safeguard the interests of the Bank and its shareholders in accordance with the provisions of Act no. 2/1995, on Public Limited Companies, Act no. 161/2002, on Financial Undertakings, and other relevant rules and guidelines respecting the activities of financial undertakings.

At the end of 2016 the Bank was wholly owned by the Icelandic Government, directly and through its subsidiary ISB Holding ehf., which is also wholly owned by the Icelandic Government. The shares are administered by ISFI in accordance with the ISFI Act. Shareholders' meetings are the general forum for informing and communicating with shareholders. In between meetings of the Bank's shareholders the Chairman of the Board, on behalf of the Board of directors, is responsible for communications with shareholders.

Shareholders can at any time express their views in relation to the operations of the Bank to the Board of Directors and submit queries to the Board for discussion.

## Information on infringements of laws and regulations that the appropriate supervisory or ruling body has determined.

On 27 October 2016 the FME and Íslandsbanki came to a settlement in respect of a violation of Article 18(1) of Act no. 108/2007 on securities transactions.

This Corporate Governance Statement was approved by Íslandsbanki's Board of Directors on 15 February 2017.