Íslandsbanki

Consolidated Financial Statements 2020

Contents

Factsheet 4Q20

Íslandsbanki

Our Profile

Íslandsbanki is a universal bank and a leader in financial services in Iceland with a history of 145 years of servicing key industries. The Bank has a 25-40% market share across all domestic business segments.

Íslandsbanki's purpose is to move Iceland forward by empowering our customers to succeed. Driven by the vision to be #1 for service, Íslandsbanki's relationship banking business model is propelled by three business divisions that manage and build relationships with the Bank's customers.

Íslandsbanki has developed a wide range of online services such as the Íslandsbanki and Kass apps, enabling customers to do their banking anywhere and anytime. At the same time, the Bank continues to operate the most efficient branch network in Iceland through its strategically located 12 branches.

Íslandsbanki has a BBB/A-2 rating from S&P Global Ratings.

The Bank

12 branches

745 number of FTEs at Íslandsbanki at year-end

Sustainability

- First Icelandic bank to develop Sustainable Financing Framework
- First sustainable bond by an Icelandic bank
- Member of a global Partnership for Carbon Accounting Financials (PCAF)

Digital milestones

- Increased app usage across all customer segments
- The first open banking feature added to the app
- Continuous growth in new and refinanced mortgages through automated digital channels

Market share*

32% retail customers

35% SMEs

35% large companies

Ratings and certifications

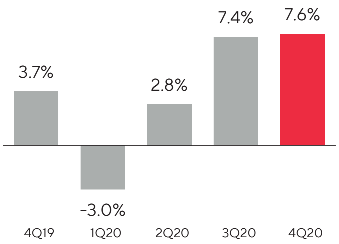
S&P Global Ratings

BBB/A-2 Stable outlook

EQUAL PAY CERTIFICATE 2018 - 2021

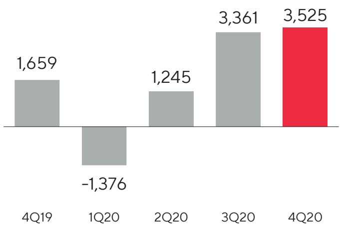
EXEMPLARY IN CORPORATE GOVERNANCE

Return on equity

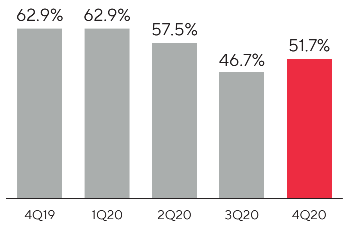


Profit (loss) after tax

(ISKm)

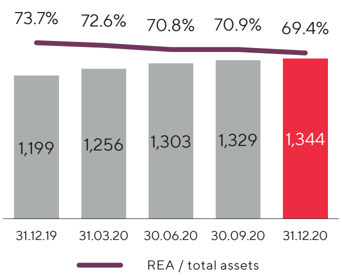


Cost / income ratio



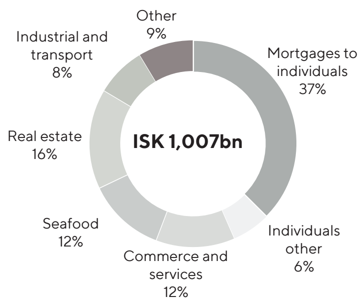
Total assets

(ISKbn)



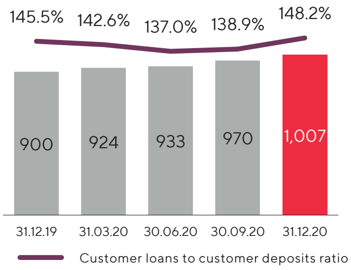
Loans to customers

(Sector split as of 31.12.20)

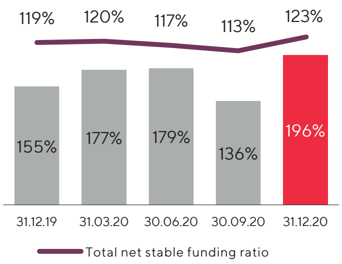


Loans to customers

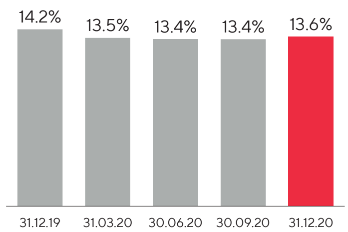
(ISKbn)



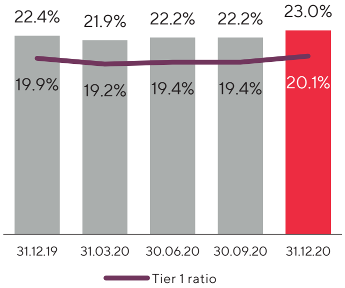
Total liquidity coverage ratio



Leverage ratio



Total capital ratio



The information above has not been reviewed or audited by the Bank's auditor

*Based on Gallup surveys regarding primary bank

Directors' Report

The audited consolidated financial statements of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") for the year 2020 comprise the financial statements of Íslandsbanki hf. and its subsidiaries, together referred to as "the Group".

Operations in 2020

Íslandsbanki is a universal bank offering comprehensive financial services to households, corporations, and institutional investors in Iceland. The Group is one of Iceland's largest banking and financial services groups, with a strong domestic market share. The vision is to make Íslandsbanki #1 for service.

The profit from the Group's operations for the year 2020 amounted to ISK 6,755 million, which corresponds to 3.7% return on equity. The Board of Directors proposes that ISK 3.4 billion will be paid in dividends to shareholders, which is 50% of profits in 2020 and is in line with the Bank's policy of paying dividends of 40-50% of the profit of the year. The Board may convene a special shareholders' meeting later in the year to propose payment of additional dividends if the Bank's accumulated capital reserves are considered to exceed its long-term capital requirements. Due to uncertainties regarding the impact of the COVID-19 pandemic on the Icelandic economy and views expressed by the Icelandic government and regulator, the Bank did not pay any dividends in 2020. At year-end 2020 the Group employed 779 full-time members of staff, including 745 within the Bank itself, 57% female and 43% male.

Net interest income increased by 1.7% between years, as the balance sheet growth is somewhat offset by a lower interest environment, resulting in a drop of 0.1 percentage points in the net interest margin. Net fee and commission income was down by 3.4%. Other net operating income was an ISK 743 million loss due to negative net financial income. Administrative expenses were down by 7.1% between years. Salary costs were down by 7.9% as the number of FTE's reduced. Other operating expenses decreased by 6.1% and there was also a substantial reduction in both the Bank tax and the contribution to the Depositors' and Investors' Guarantee Fund. Net impairments were negative by ISK 8.8 billion. The large increase in the cost of risk almost entirely related to the impact of the COVID-19 pandemic on the corporate loan book.

The balance sheet of the Group grew by 12.1% between years following a 11.9% growth in loans to customers, due to a 28% increase in loans to individuals. The increased market share in mortgages was partly the result of the lower interest rate environment and reduced lending presence from pension funds. The ratio of non-performing loans decreased from 3.0% to 2.9% during the year. Loans in stage 2 under IFRS-9 increased from 2.6% to 15.6%, as most exposures to the tourism sector evidenced an increased risk of default and are in many cases subject to forbearance measures due to the COVID-19 pandemic.

Deposits from customers increased by 9.9% in 2020, driven by growth in all business units, where the biggest growth of 24.5% was in Corporate and Investment Banking. The Bank was successful overall in its funding operations in 2020. Covered bonds amounting to ISK 30.9 billion were issued through regular auctions throughout the year. In late April 2020 S&P lowered the Bank's rating to BBB/A-2 with a stable outlook from previous BBB+/A-2 with a negative outlook. The other large Icelandic banks were downgraded at the same time and in all cases the downgrade was reasoned to be due to weaker business prospects and the effect of the COVID-19 pandemic.

The Group's total equity amounted to ISK 186.2 billion and total assets were ISK 1,344.2 billion at year-end and the Group's total capital ratio was 23%. The Bank's regulatory capital requirement was reduced in 2020 as the countercyclical buffer was lowered from 2.0% to zero, as a result of economic uncertainties relating to the COVID-19 pandemic. The current capital requirement is therefore 17.0% and well below the Bank's capital ratio. The Bank's liquidity position remains strong and well above regulatory requirements.

The COVID-19 pandemic has been the main theme of the year, both due to the impact on many of the Bank's customers and also on the operations of the Bank itself. Our employees have worked from home large parts of the year, which has not affected efficiency and we saw record positive numbers in the annual staff satisfaction survey. As the period of limited personal interactions continues to lengthen, it can however be expected that staff members start to show strain and a strong hope for a new normal, where they can spend at least 3-4 days a week in the office.

The COVID-19 pandemic has also had a dramatic impact on branch openings, and we have seen a large uptake in the use of other service channels. Visits to branches have declined by over 70% in the past few years. Concurrent with these changes, the branches at Höfði and Grandi have been merged with the Laugardalur branch. After the merger, the Bank will operate three branches in the capital area.

Íslandsbanki has in 2020 put an even stronger focus than before on sustainability. In the fourth quarter Íslandsbanki was the first bank in Iceland to publish a Sustainable Financing Framework. Based on this new framework, the Bank also became the first bank in Iceland to issue sustainable bonds. Firstly, a EUR 300 million sustainable benchmark bond was issued internationally and was close to four times oversubscribed. Secondly, an ISK 2.7 billion domestic green bond was sold to Icelandic investors. The Bank has begun to make use of these funds and extended its first green loan in December 2020.

Outlook

The Icelandic economy was unavoidably hard hit by the COVID-19 pandemic in 2020, given the size of its tourist sector as share of both export revenues and the labour market. Gross domestic product (GDP) contraction in 2020 looks likely to prove over 8%, making the year the worst in this regard in Iceland's modern economic history. Around 2/3 of the GDP fall is due to declining exports and 1/3 caused by a fall in domestic demand. However, economic policy has mitigated the impact on households and businesses considerably as monetary conditions have been eased and fiscal spending substantially increased to facilitate support measures for the afflicted sector and boost public investment.

Directors' Report

As a result, the rise in defaults and bankruptcies has been more muted than feared and the majority of Icelandic households have been spared a significant fall in disposable income.

The duration of the economic setback will hinge on how rapidly travel conditions normalise and global economic activity resumes. The rapid process of the development and rollout of vaccines so far has gradually increased the upside potential for economic rebound in Iceland. Assuming fading impact from the COVID-19 pandemic over the coming months, there is a good probability of a return to healthy GDP growth in the latter half of 2021. The Bank's Chief economist expects GDP growth to average 3.2% in 2021, driven by increasing exports as well as a boost to public investment and moderate consumption growth. For 2022, the expected 5.0% GDP growth will be largely driven by increasing domestic demand.

There is still considerable uncertainty regarding the overall impact of the COVID-19 pandemic on the tourism industry in Iceland and especially whether visitor numbers will pick up rapidly in 2021. Supporting the Bank's customers through this recession will remain the key focus for the coming months. As the economy improves, the focus will shift more towards improving profitability and managing both the cost base and growth in the balance sheet and revenue. The work environment for the Bank's employees can be expected to move towards a new normal, where employees spend a part of the week working from home. The Bank's financial strength has remained robust throughout the recent economic challenges and the Bank is well placed to continue to be #1 for service for its customers.

Risk management

The Bank is exposed to various risks. The management of these risks is an integral part of the Bank's operations and the Bank has focused on building up a responsible internal risk culture among the Bank's employees. The ultimate responsibility for ensuring an adequate risk management framework lies with the Board of Directors. The Board defines and communicates the acceptable level of risk through the Bank's risk management policies and the CEO is responsible for ensuring that risks are managed within those limits.

The Board hereby declares that Íslandsbanki has an overall satisfactory risk management in relation to the Bank’s profile and strategy.

The Bank's risk management framework and policies are discussed under Notes 46-66 to the consolidated financial statements and in the unaudited Pillar 3 Report.

Ownership

The Bank is wholly owned by the Icelandic Government and there were no changes in the ownership in 2020. The shares are administered by the Icelandic State Financial Investments (ISFI) in accordance with Act no. 88/2009 on Icelandic State Financial Investments.

The Icelandic Government published in February 2020 an updated general ownership policy for financial institutions with regards to ownership stakes administered with the Icelandic State Financial Investments (ISFI). In December 2018 the Bank signed an agreement with ISFI on general and specific goals for the operations, in line with article 2.3 of the ownership policy.

The Minister of Finance and Economic Affairs has made a formal decision to initiate the process of the sale of shares in Íslandsbanki in accordance with the ISFI (Icelandic State Financial Investments) proposal dated 17 December 2020. The ISFI is tasked with preparing Íslandsbanki for a listing on a local regulated stock market and the consequent sale of shares in a public offering (IPO) with the aim of a distributed ownership and the minimum of 25% of shares and a maximum of 35% of shares to be sold.

Corporate governance

The Board of Directors of Íslandsbanki is committed to excellence in its governance framework so that it complies with the best corporate governance practices in the financial market at all times.

Íslandsbanki was first recognised as “Exemplary in Corporate Governance” in March 2014. The recognition was awarded following a comprehensive review of the practices of the Board, Board subcommittees and management. The recognition has been renewed annually since and is now granted by Stjórnvísi.

The Board of Directors comprises seven non-executive directors and one alternate member. The Board undertakes the Bank's affairs and is responsible for setting the Bank's general strategy as well as instructing the CEO on its further implementation and execution. The Board has a supervisory role overseeing that the Bank's organisation and activities are at all times in accordance with relevant laws, regulations and good business practices. Furthermore, the Board shall monitor the execution of its policies, the sound control of accounting and financial management, and ensure that group internal audit, compliance, risk management and internal controls are effective at all times.

Candidates for board membership are nominated through a selection process administered by the Icelandic State Financial Investments in accordance with Article 7 of the ISFI Act no. 88/2009. At the Bank's Annual General Meeting in March the Board of Directors was elected for the Bank. 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 consists of seven members, four female and three male.

The Board has approved a policy on the suitability of the Board of Directors, the CEO and key function holders. The policy states, among other things, that the composition of the Board shall at any time be diverse, with regard to educational and professional background, gender and age.

Directors' Report

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 CEO is responsible for the day-to-day operations of the Bank and that the Bank's business is, at all times, in accordance with the Bank's Articles of Association, policies of the Board and the relevant law. The CEO engages the Bank's Compliance Officer and appoints members of the Executive Committee and other Senior Management Committees.

The Executive Committee, comprising seven members, including the CEO, is composed of three women and four men. The role of the Executive Committee is to maintain an overall view of the Bank's operations and to coordinate key aspects of its activities that are not supervised by other senior management committees. The CEO ensures that the Board is regularly provided with accurate information on the Bank's finances, development and operations.

The Bank's Finance division is responsible for the preparation of the Group's consolidated financial statements which are prepared in accordance 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 the second quarter interim consolidated financial statements and audit annual consolidated financial statements.

The regulatory framework for corporate governance practices within Íslandsbanki consists of the law applicable to its operations, including those imposed by the Central Bank of Iceland and Nasdaq Iceland. The applicable laws include, inter alia, the Act on Financial Undertakings no. 161/2002, the Act on Securities Transactions no. 108/2007, the Act on Public Limited Companies no. 2/1995 and the Act on Competition no. 44/2005, available on the Icelandic legislature's website (www.althingi.is).

The Board of Directors follows the Corporate Governance Guidelines (5th ed.) issued by the Iceland Chamber of Commerce, Nasdaq Iceland and SA-Business Iceland, available on www.corporategovernance.is (hereinafter the Guidelines). The Bank's practices are compliant with the guidelines except for Article 1.5. Article 1.5 of the Guidelines provides that 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 ISFI in accordance with article 7 of the ISFI Act.

A more detailed description of Íslandsbanki's governance framework and associated practices can be found in the Bank's Corporate Governance Statement enclosed in an unaudited Appendix to the consolidated financial statements and on the Bank's website, www.islandsbanki.is.

Sustainability

Íslandsbanki's Sustainability Policy was approved by its board in late 2019. The Policy aims at making the Bank a model of exemplary operations in the Icelandic business community, based on internationally recognised environmental, social, and governance (ESG) criteria. The ESG criteria are a set of references used by investors to evaluate investments based on responsible investment methodology.

The Bank aims to be a leader in the area of sustainable development and a catalyst for positive social action, moving Iceland forward by empowering its customers to succeed. To this end, the Bank intends to initiate broad collaboration on responsible business practices that both contribute to sustainable development in the Icelandic economy and support the Government's Climate Action Plan, while also supporting the UN SDGs.

Alongside its vision of being a leader in service to customers, the Bank will focus on integrating sustainability considerations into its activities, in addition to its profit objectives. The Bank will take account of ESG criteria in its risk management and will explore opportunities to take advantage of green investment opportunities. Íslandsbanki aims to increase the general public's financial knowledge and interest in the subject and, to this end, it offers interesting and accessible seminars on finance and economics.

Íslandsbanki's Sustainability Policy creates a comprehensive framework for its activities in the area of environmental affairs, respect for human rights, responsible lending, investments, purchasing, and grants, as well as integrating with and supporting the Bank's other policies. Íslandsbanki sets quantifiable ESG targets in its operations and discloses its performance relative to targets, in accordance with the Nasdaq ESG Guidelines and relevant GRI standards, in a separate report issued concurrent with the Bank's annual financial statements. When calculating the Bank's carbon footprint, all greenhouse gas (GHG) emissions for its operations were examined, whether direct emissions from its procedures or emissions from employees, suppliers, contractors or customers. Reported emissions are divided into scopes 1, 2 and 3. Íslandsbanki's Sustainability Report for the year 2020 was reviewed and signed by Klappir Green Solutions. The report is based on information collected by the company's environmental software, EnviroMaster, throughout the year. The Sustainability Report includes the key information on the environmental, social and governance criteria for Íslandsbanki in accordance with the Nasdaq ESG guidelines from 2019.

Íslandsbanki has in place a Code of Conduct for employees and the Board of Directors which is available on the Bank's website and in addition the Bank's Sustainability Policy emphasises these matters. The Code's aim is to promote good operational practices, reporting of misconduct and actions to prevent conflict of interest. Employees confirm annually that they have read and understood the rules and commit their adherence to the rules, and at the end of 2020 more than 99% of employees had confirmed the rules. Moreover, the Bank has in place an extensive policy on actions against money laundering and terrorist financing. The Bank emphasises respect for human rights and avoids business transactions where human rights are violated, including discrimination on the basis of gender, religion, or race according to the Sustainability Policy and the Code of Conduct for suppliers.

Directors' Report

As a signatory to the UN Global Compact, Íslandsbanki is committed to aligning its operations and strategies with 10 principles covering human rights, labour, the environment and anti-corruption. In 2020, the Bank joined the UN Principles for Responsible Banking, which provide a framework for a sustainable banking system, and help the industry to demonstrate how it makes a positive contribution to society and build on the following six principles: Alignment, Impact and Target Setting, Clients and Customers, Stakeholders, Governance and Culture, and Transparency and Accountability. The Bank has in place a Code of Conduct and a Conflict of Interest Policy in order to ensure creditability in business transacted by the Bank and its clients and employees' impartiality in handling and processing individual cases. The Bank has in place a Code of Conduct for Suppliers, approved in June 2020, which are based on ESG criteria. The Bank is committed to engage in active dialogue with its suppliers on enhancing their focus on sustainable business practices. In October 2020, Íslandsbanki became the first Icelandic bank to develop and publish a Sustainable Financing Framework for sustainable loans in its portfolio, with a second party opinion from Sustainalytics. This enabled the Bank to issue the first sustainable and green bonds by an Icelandic bank in late 2020.

In line with the Policy, the Bank has approved seven sustainability goals for its operations, to be completed by 2025. The goals are based on ESG criteria and include among others plans for the Bank to become carbon neutral in its operations, thereof reducing carbon emissions by 50% from 2019 to year-end 2024. The goals are supported by annual targets set by business units as part of their 5-year planning process. The Bank joined in 2020 a coalition of other banks, that are developing a methodology to measure carbon emissions from its lending and investment operations, called the Partnership for Carbon Accounting Financials (PCAF).

During the year the Board of Directors approved an updated version of the Risk Appetite Statement and for the first-time sustainability risk is discussed. One of the Bank's seven sustainability goals is to measure and publish on the sustainability risk and strengthen the sustainability frame. This is emphasis is reflected in the Bank's unaudited Pillar 3 Report 2020 which has a chapter on sustainability and climate risk adhering to international TCFD (Task Force on Climate-related Financial Disclosures) criteria.

The Board of Directors has approved the Sustainability Policy and sets the Bank's strategy and risk appetite in terms of sustainability risk. The Board is regularly updated on corporate sustainability matters and the usage of the Bank's Sustainable Financing Framework. The Corporate Governance and Human Resource subcommittee of the Board assists the Board in fulfilling its oversight responsibilities concerning sustainability.

The CEO is responsible for executing the strategy and has appointed a Sustainability Committee as a main building block of the governance structure. The Committee is the formal forum for discussions on all issues related to sustainability risk, sustainable procurement and business opportunities. The Committee is independent from credit committees and needs to approve proposals for credit cases before they are included in the Sustainable Financing Framework. The Committee has senior representatives from business units, Finance and Risk Management.

The Bank's sustainability and ESG factors are further described in the unaudited annual and sustainability report and the Bank's unaudited Pillar 3 report for the year 2020.

Statement by the Board of Directors and the CEO

The audited consolidated financial statements for the year ended 31 December 2020 have been prepared on a going concern basis in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union; the Act on Annual Accounts, no. 3/2006; the Act on Financial Undertakings, no. 161/2002; and rules on accounting for credit institutions, where applicable.

To the best of our knowledge, these consolidated financial statements provide a true and fair view of the Group's operating profits and cash flows in 2020 and its financial position as of 31 December 2020. Furthermore, in our opinion the financial statements and the Director's report give fair view of the main operational developments and achievements and describe the principal risks and uncertainties that the Group faces in its operations.

The Board of Directors and the CEO have today discussed and approved the 2020 Consolidated Financial Statements of Íslandsbanki.

Kópavogur, 10 February 2021

Board of Directors:
Hallgrímur Snorrason, Chairman
Heiðrún Jónsdóttir, Vice-Chairman
Anna Þórðardóttir
Árni Stefánsson
Frosti Ólafsson
Guðrún Þorgeirsdóttir
Herdís Gunnarsdóttir

Chief Executive Officer:
Birna Einarsdóttir

EY
Building a better working world

Independent Auditor's Report

To the Board of Directors and shareholders of Íslandsbanki hf.

Opinion

We have audited the consolidated financial statements of Íslandsbanki hf. and its subsidiaries (the Group) which comprise the consolidated statement of financial position as at 31 December 2020 and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flow for the year then ended and a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2020, and its consolidated financial performance and its consolidated cash flows for the year then ended, in accordance with the International Financial Reporting Standards, as adopted by the European Union and additional requirements in the Icelandic Act on Annual Accounts, Act on Financial Undertakings and rules on accounting for credit institutions, where applicable.

Our opinion in this report on the consolidated accounts are consistent with the content of the additional report that has been submitted to the parent company's audit committee in accordance with the Audit Regulation (537/2014) Article 11.

Basis for Opinion

We conducted our audit in accordance with the International Standards on Auditing (ISAs). Our responsibilities are further described in the Auditor's Responsibilities for the Audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the consolidated financial statements in Iceland, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

To the best of our knowledge, we have not provided any prohibited non-audit services as described in article 5(1) of Regulation (EU) no. 537/2014.

Appointment of auditor

We were initially appointed as auditor of Íslandsbanka hf. on 25 March 2015 for the financial year 2015 and we have been reappointed every year since then.

Key Audit Matters

Key Audit Matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole and in forming our opinion thereon. We do not provide a separate opinion on these matters.

We have fulfilled our responsibilities described in the "Auditor's responsibilities for the audit of the financial statements" section, including in relation to the key audit matters below. Accordingly, our audit included the design and performance of procedures to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the financial statements.

Building a better working world

Why significant	How our audit addressed the Key Audit Matter

Provision for expected credit losses (ECL)

Loans to customers represent ISK 1,006,717 million or 75% of total assets at 31 December 2020 against which impairment allowances of ISK 17,514 million have been recorded.

There is significant uncertainty about the economic impact of the COVID-19 pandemic and the impact on expected credit losses, in particular due to loans to customers in the tourism and related industries.

The determination of the provision for credit impairment is based on estimates and judgement by management. Key areas of judgement include:

- management overlays and assumptions related to the economic effects of the COVID-19 pandemic;
- the interpretation of the requirements to determine impairment under application of IFRS 9, which is reflected in the Group's expected credit loss model;
- the identification of loans with significant deterioration in credit quality;
- assumptions used in the expected credit loss model such as the financial condition of the counterparty, expected future cash flows and forward-looking macroeconomic factors.

Due to the use of judgement and estimates, in particular due to the COVID-19 pandemic, and the relative size of loans to customers on the balance sheet, we consider the provision for credit impairment a Key Audit Matter.

Our procedures focused on the following to respond to the Key Audit Matter, among others:

- Assessing the Group's expected credit loss model, focusing on the following areas:
    - alignment of the expected credit loss model and its underlying methodology with the requirements of IFRS 9;
    - approach to the incorporation of forward-looking macroeconomic factors;
    - management overlays and assumptions related to the economic effects of COVID-19 pandemic on the expected credit loss model;
- Testing the effectiveness of relevant controls relating, among others, to the:
    - data used to determine the provision for credit impairment, including transactional data captured at loan origination and ongoing internal credit quality assessment;
    - expected credit loss model, including model build and approval, ongoing monitoring/validation, model governance and mathematical accuracy;
    - review and approval of forward-looking macro-economic factors; and
    - registration and valuation of collateral used in the calculation of expected credit loss.
- Testing of a sample of loans and procedures to evaluate among others:
    - timely identification of loans with significant deterioration in credit quality;
    - expected loss calculation by re-performing and assessing the reasonableness of the ECL model calculations;
    - appropriateness of forward-looking macroeconomic factors; and
    - COVID-19 pandemic effects of a sample of borrowers in the tourism and related industries and impact on collateral.

In addition, we assessed the adequacy of the disclosures in the consolidated financial statements. Refer to Notes 3 and 67.4 for credit impairment.

Building a better working world

Why significant	How our audit addressed the Key Audit Matter
Reliability of information from IT systems relevant to financial reporting	
The Group is highly dependent on IT systems due to the significant number of transactions that are processed daily and the complexity of the various systems used by the Group. In the process of preparing the consolidated financial statements the Group uses data from many complex IT systems. The reliability of the data, among others, the accuracy and completeness, is important to support the reliability of financial reporting. Because of the importance of the data from the IT systems supporting the financial reporting we consider their reliability a Key Audit Matter.	Our procedures focused on the following to respond to the Key Audit Matter, among others: • Obtained an understanding of the Group's IT systems and the IT-environment relevant for financial reporting. • Reviewed the design, implementation and effectiveness of control activities, as appropriate, related to change management, access management and computer operations for the systems considered important for the audit. • For those systems, considered important in the audit and are outsourced, we obtained and assessed the ISAE 3402 report which is issued by the services organisation and reviewed by an independent auditor. IT specialists were involved in the audit.

We have fulfilled our responsibilities described in the "Auditor's responsibilities for the audit of the consolidated financial statements" section, including in relation to the Key Audit Matters above. Accordingly, our audit included the design and performance of procedures to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters above, provide the basis for our audit opinion on the consolidated financial statements.

Other information

This document also contains other information than the consolidated financial statements and our auditor's report thereon. The other information is: The unaudited highlights, Directors´ Report, unaudited quarterly statements in Note 7 and unaudited Íslandsbanki's Corporate Governance Statement 2020 in appendix. Management and Board of Directors are responsible for the other information.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon except for confirmation regarding Directors' Report as stated below.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether it is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we, based on the work we have performed concerning this other information, conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of CEO and Board of Directors for the consolidated financial statements

The Chief Executive Officer (CEO) and Board of Directors are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards, as adopted by the European Union and additional requirements in the Icelandic Act on Annual Accounts, Act on Financial Undertakings and rules on accounting for credit institutions, where applicable.

The CEO and Board of Directors are responsible for such internal control that management determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

The Board of Directors is responsible for overseeing the Group's consolidated financial reporting process.

Auditor's Responsibilities for the Audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with International Standards on Auditing

(ISAs) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with the International Standards on Auditing (ISAs), we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the Key Audit Matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on the Board of Directors Report

Pursuant to the legal requirements of Article 104, Paragraph 2 of the Icelandic Financial Statement Act no. 3/2006, we confirm that, to the best of our knowledge, the report of the Board of Directors accompanying the consolidated financial statements includes all information required by the Icelandic Financial Statement Act.

Reykjavík, 10 February 2021

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Margrét Pétursdóttir
State Authorised Public Accountant

Ernst & Young ehf.
Borgartúni 30
105 Reykjavík

Consolidated Income Statement

	Notes	2020	2019
Interest income*		55,695	61,965
Interest expense		(22,324)	(29,143)
Net interest income	8	33,371	32,822
Fee and commission income		12,651	12,052
Fee and commission expense		(2,126)	(1,153)
Net fee and commission income	9	10,525	10,899
Net financial expense	10	(1,391)	(820)
Net foreign exchange gain	11	451	139
Other operating income	12	197	2,125
Other net operating income		(743)	1,444
Total operating income		43,153	45,165
Salaries and related expenses	13	(12,917)	(14,019)
Other operating expenses	14	(9,829)	(10,469)
Contribution to the Depositors' and Investors' Guarantee Fund		(679)	(936)
Bank tax	67.20	(1,588)	(3,528)
Total operating expenses		(25,013)	(28,952)
Profit before net impairment on financial assets		18,140	16,213
Net impairment on financial assets	15	(8,816)	(3,480)
Profit before tax		9,324	12,733
Income tax expense	16	(2,472)	(3,909)
Profit for the year from continuing operations		6,852	8,824
Discontinued operations, net of income tax	17	(97)	(370)
Profit for the year		6,755	8,454
Profit attributable to shareholders of Íslandsbanki hf.		7,061	8,809
Loss attributable to non-controlling interests		(306)	(355)
Profit for the year		6,755	8,454
Earnings per share from continuing operations			
Basic and diluted earnings per share attributable to the shareholders of Íslandsbanki hf.	18	0.72	0.92

*Of which interest income amounting to ISK 53,378 million (2019: ISK 59,289 million) is calculated using the effective interest method.

Before its sale on 7 July 2020, the subsidiary Borgun hf. was classified as disposal group held for sale and as discontinued operations, accordingly the comparative figures have been restated (see Note 5).

The notes on pages 17 to 88 are an integral part of these Consolidated Financial Statements.

Íslandsbanki hf. Consolidated Financial Statements 2020 11 Amounts are in ISK million

Consolidated Statement of Comprehensive Income

	2020	2019
Profit for the year	6,755	8,454
Net gain on financial assets	114	1,272
Net gain (loss) on financial liabilities	108	(677)
Items that will not be reclassified to the income statement	222	595
Foreign currency translation	(329)	-
Items that may subsequently be reclassified to the income statement	(329)	-
Other comprehensive income (expense) for the year, net of tax	(107)	595
Comprehensive income for the year	6,648	9,049

Total comprehensive income attributable to shareholders of Íslandsbanki hf.	7,492	8,939
Total comprehensive income (expense) attributable to non-controlling interests	(844)	110
Total comprehensive income for the year	6,648	9,049

The notes on pages 17 to 88 are an integral part of these Consolidated Financial Statements.

Íslandsbanki hf. Consolidated Financial Statements 2020 12 Amounts are in ISK million

Consolidated Statement of Financial Position

	Notes	31.12.2020	31.12.2019
Assets			
Cash and balances with Central Bank	23	78,948	146,638
Loans to credit institutions	24	89,920	54,376
Bonds and debt instruments	19	128,216	52,870
Derivatives	25	6,647	5,621
Loans to customers	26	1,006,717	899,632
Shares and equity instruments	19	14,851	18,426
Investments in associates	28	775	746
Property and equipment	29	7,341	9,168
Intangible assets	30	3,478	4,330
Other assets	31	4,125	6,608
Non-current assets and disposal groups held for sale	32	3,173	1,075
Total Assets		1,344,191	1,199,490
Liabilities			
Deposits from Central Bank and credit institutions	33	39,758	30,925
Deposits from customers	34	679,455	618,313
Derivative instruments and short positions	25	6,936	6,219
Debt issued and other borrowed funds	36	387,274	306,381
Subordinated loans	37	27,194	22,674
Tax liabilities	39	5,450	7,853
Other liabilities	40	11,920	27,063
Total Liabilities		1,157,987	1,019,428
Equity			
Share capital		10,000	10,000
Share premium		55,000	55,000
Reserves		6,181	7,065
Retained earnings		113,529	105,569
Total Shareholders' Equity		184,710	177,634
Non-controlling interests		1,494	2,428
Total Equity		186,204	180,062
Total Liabilities and Equity		1,344,191	1,199,490

The notes on pages 17 to 88 are an integral part of these Consolidated Financial Statements.

Íslandsbanki hf. Consolidated Financial Statements 2020 13 Amounts are in ISK million

Consolidated Statement of Changes in Equity

	Share capital	Share premium	Statutory reserve	Restricted reserves	Fair value reserve	Liability credit reserve	Foreign currency translation reserve	Retained earnings	Total shareholders' equity	Non-controlling interests	Total equity
Equity as at 1.1.2020	10,000	55,000	2,500	3,525	1,432	(392)	-	105,569	177,634	2,428	180,062
Profit (loss) for the year								7,061	7,061	(306)	6,755
Net gain (loss) on financial assets					(860)			1,392	532	(418)	114
Net gain (loss) on financial liabilities						154		(46)	108		108
Foreign currency translation							(209)		(209)	(120)	(329)
Restricted due to capitalised development costs				(291)				291	-		-
Restricted due to fair value changes				282				(282)	-		-
Restricted due to associates				40				(40)	-		-
Changes due to IFRS 15								(115)	(115)		(115)
Changes in non-controlling interests								(301)	(301)	(90)	(391)
Equity as at 31.12.2020	10,000	55,000	2,500	3,556	572	(238)	(209)	113,529	184,710	1,494	186,204
Equity as at 1.1.2019	10,000	55,000	2,500	3,750	625	(376)	-	102,496	173,995	2,318	176,313
Profit (loss) for the year								8,809	8,809	(355)	8,454
Dividends paid								(5,300)	(5,300)		(5,300)
Net gain on financial assets					807				807	465	1,272
Net loss on financial liabilities						(16)		(661)	(677)		(677)
Restricted due to capitalised development costs				(551)				551	-		-
Restricted due to fair value changes				308				(308)	-		-
Restricted due to subsidiaries and associates				18				(18)	-		-
Equity as at 31.12.2019	10,000	55,000	2,500	3,525	1,432	(392)	-	105,569	177,634	2,428	180,062

Authorised share capital of the Bank is 10,000 million ordinary shares of ISK 1 each. At year-end 2020 paid up share capital totalled ISK 65,000 million which is the total stated share capital of the Bank. The Bank has one class of ordinary shares which carry no right to fixed income. The Annual General Meeting ("AGM") for the operating year 2019 was held on 19 March 2020. At the AGM shareholders approved the Board’s proposal that dividends to shareholders for the operating year 2019 shall not be paid based on the current economic environment.

The notes on pages 17 to 88 are an integral part of these Consolidated Financial Statements.

Íslandsbanki hf. Consolidated Financial Statements 2020 14 Amounts are in ISK million

Consolidated Statement of Cash Flows

	Notes	2020	2019
Profit for the year		6,755	8,454
Non-cash items included in profit for the year*		28,780	24,324
Changes in operating assets and liabilities*		(109,535)	(7,998)
Dividends received		30	46
Income tax and bank tax paid		(6,754)	(6,493)
Net cash (used in) provided by operating activities		(80,724)	18,333
Net investment in a subsidiary		(2,176)	-
- thereof proceeds from sale of a subsidiary		2,384	-
- thereof cash and cash equivalents owned by a subsidiary sold during the year		(4,560)	-
Proceeds from sales of property and equipment		24	21
Purchase of property and equipment		(552)	(327)
Purchase of intangible assets		(260)	(246)
Net cash used in investing activities		(2,964)	(552)
Proceeds from borrowings		80,778	112,105
Repayment and repurchases of borrowings		(33,673)	(114,708)
Repayment of lease liabilities		(390)	(378)
Dividends paid		-	(5,300)
Net cash provided by (used in) financing activities		46,715	(8,281)
Net increase (decrease) in cash and cash equivalents		(36,973)	9,500
Effects of foreign exchange rate changes		160	(222)
Cash and cash equivalents at the beginning of the year		152,481	143,203
Cash and cash equivalents at year-end		115,668	152,481

Reconciliation of cash and cash equivalents			
Cash on hand	23	3,814	4,403
Cash balances with Central Bank	23	75,134	142,235
Bank accounts	24	46,269	21,122
Mandatory reserve, special restricted and pledged balances with Central Bank	23	(9,549)	(15,279)
Cash and cash equivalents at year-end		115,668	152,481

*For further breakdown see the following page.

The Group has prepared its consolidated statement of cash flows using the indirect method. The statement is based on the net profit after tax for the year and shows the cash flows from operating, investing and financing activities and the increase or decrease in cash and cash equivalents during the year.

The Group presents a statement of cash flows that includes an analysis of all cash flows in total, including both continuing and discontinued operations (see Note 5).

Interest received in 2020 amounted to ISK 49,410 million (2019: ISK 60,624 million) and interest paid in 2020 amounted to ISK 20,455 million (2019: ISK 22,736 million). Interest is defined as having been paid when it has been deposited into the customer account and is available for the customer's disposal.

The notes on pages 17 to 88 are an integral part of these Consolidated Financial Statements.

Íslandsbanki hf. Consolidated Financial Statements 2020 15 Amounts are in ISK million

Consolidated Statement of Cash Flows

	2020	2019
Depreciation, amortisation and write-offs	1,765	1,960
Share of profit of associates	(45)	(64)
Accrued interest and fair value changes on debt issued and subordinated loans	12,621	11,450
Net impairment on financial assets	9,056	3,568
Foreign exchange gain	(387)	(143)
Net (gain) loss from sales of a subsidiary, property and equipment	(427)	17
Unrealised fair value loss recognised in profit or loss	1,545	192
Discontinued operations, net of income tax	524	125
Bank tax	1,588	3,528
Income tax	2,472	3,682
Other changes	68	9
Non-cash items included in profit for the year	28,780	24,324

Mandatory reserve, special restricted and pledged balances with Central Bank	5,730	1,833
Loans to credit institutions	(7,725)	(15,268)
Bonds and debt instruments	(73,163)	17,254
Loans to customers	(100,076)	(52,638)
Shares and equity instruments	(885)	(3,953)
Other assets	(995)	1,644
Non-current assets and liabilities held for sale	1,168	3
Deposits from Central Bank and credit institutions	7,714	15,232
Deposits from customers	51,984	37,678
Derivative instruments and short positions	8,942	(2,944)
Other liabilities	(2,229)	(6,839)
Changes in operating assets and liabilities	(109,535)	(7,998)

Non-cash transactions 2020

During the year Íslandsbanki sold its 63.5% stake in Borgun hf. (see Note 5). ISK 415 million of the sale price is due in 2021. Prior to the sale, shares in BVS ehf. a company holding series C preferred shares in Visa Inc., which were not part of the sale of Borgun hf., were transferred to the old owners of Borgun hf.

During the year the Bank sold an office building for the price of ISK 100 million with ISK 85 million outstanding at the end of the year.

Non-cash transactions 2019

During the year the Bank repurchased own debt securities amounting to ISK 4,319 million by issuing new debt.

The Group recognised right-of-use assets amounting to ISK 4,505 million and the same amount in lease liabilities following the adoption of IFRS 16 - Leases.

The notes on pages 17 to 88 are an integral part of these Consolidated Financial Statements.

Íslandsbanki hf. Consolidated Financial Statements 2020 16 Amounts are in ISK million

Notes to the Consolidated Financial Statements

Notes to the Consolidated Financial Statements

1. Corporate information

Íslandsbanki hf., the parent company, was incorporated on 8 October 2008 and is a limited liability company domiciled in Iceland. The address of its registered office is Hagasmári 3, 201 Kópavogur, Iceland.

The consolidated financial statements for the year ended 31 December 2020 ("the consolidated financial statements") comprise the financial statements of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries together referred to as "the Group".

At the end of 2020 the Bank was wholly owned by the Icelandic Government. The shares are administered by the Icelandic State Financial Investments in accordance with Act no. 88/2009 on Icelandic State Financial Investments.

The Group provides a wide range of financial services such as retail banking, corporate banking, investment banking, wealth management and asset financing. The Group operates mainly in the Icelandic market.

The consolidated financial statements were approved and authorised for issue by the Board of Directors and the CEO of Íslandsbanki hf. on 10 February 2021.

2. Basis of preparation

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union and additional requirements in the Act on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions.

The consolidated financial statements are presented in Icelandic króna (ISK), which is the functional currency of Íslandsbanki hf. All amounts presented in ISK have been rounded to the nearest million, except when otherwise indicated. At year-end 2020 the exchange rate of the ISK against the USD was 127.21 and 156.10 for the EUR (year-end 2019: USD 121.10 and EUR 135.83).

The Group's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue in business for the foreseeable future. Therefore, the consolidated financial statements have been prepared on a going concern basis.

Basis of measurement

The consolidated financial statements are prepared on a historical cost basis, except for the following assets and liabilities, which are measured at fair value: bonds and debt instruments, shares and equity instruments, short positions in listed bonds, derivative financial instruments, and certain bonds issued by the Group.

Recognised financial liabilities designated as hedged items in qualifying fair value hedge relationships are measured at amortised cost adjusted for changes in fair value attributable to the risk being hedged.

Non-current assets and disposal groups held for sale are measured at the lower of its carrying amount and fair value less costs to sell.

3. Significant accounting estimates and judgements

The preparation of the consolidated financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses recognised. Key sources of estimation uncertainty include the allowance for credit losses, the determination of fair value of financial instruments and intangible assets. Actual results may differ from those estimates.

Estimates and underlying assumptions are under constant review. Changes in accounting estimates are recognised when they occur.

The COVID-19 pandemic continues to evolve and the economic environment in which the Group operates could continue to negatively impact the Group's financial results. The current environment, particularly, requires judgements and estimates in certain areas. The Group closely monitors the changing conditions and their impact.

Impairment of financial assets

The main assumptions used for calculating the allowance for credit losses that are subject to significant judgement include the following:

- Probability of default (PD), loss given default (LGD) and exposure at default (EAD)
- Macroeconomic variables for multiple scenarios build on available information
- Assessment of significant increase in credit risk

3. Cont'd

The probability of default (PD), exposure at default (EAD), and loss given default (LGD) inputs used to estimate expected credit losses are modelled based on variables that are most closely related with credit losses in the relevant portfolio. This includes macroeconomic variables, demographic variables, variables related to past payment history among other variables. These variables are sourced both internally and externally. Significant judgements required for measuring expected credit loss (ECL) include the following:

- Determining criteria for assessing what constitutes a significant increase in credit risk
- Establishing the forward-looking scenarios and their relative weightings
- Choosing appropriate models and assumptions for the measurement of ECL

The Group has made temporary changes to the impairment model due to the COVID-19 pandemic.The Group's impairment process allows for temporary changes to the impairment model to account for circumstances when it becomes evident that existing or expected risk factors have not been appropriately considered in the credit risk rating or modelling process. The COVID-19 pandemic has created such circumstances for the tourism industry and therefore an adjustment is warranted.To account for the material uncertainty in the operating environment of companies in the tourism industry, not reflected in their current risk class, they have been further classified into four impact groups as described in Note 51. Where the increase was found to be significant (groups 2-4), the exposure was transferred to Stage 2. In addition, an overlay factor was applied to the expected credit loss, comparable to an increase in up to three risk classes, and a higher haircut was applied to value of collateral for the higher impact groups in the more severe scenarios. The common risk factor in tourism was found to apply to loans to customers with a net carrying amount of ISK 94,202 million and the cumulative effect of the stage transfer and credit loss overlay amounted to ISK 6,115 million (see Note 15).

The All Risk Committee determined that it was appropriate to adjust the weights of the scenarios due to the COVID-19 pandemic, generally the scenarios are weighted 25%-50%-25% (good, base, bad) but it was determined appropriate to set the weights at 15%-55%-30%, as this would best represent the probability-weighted average over all possible scenarios. When deciding on the appropriate weights for the three scenarios, management used sensitivity analysis that indicated that a shift of 5% weight from the baseline to the pessimistic scenario would increase the impairment allowance by ISK 500 million while a 5% shift from the baseline to the optimistic scenario would in decrease the allowance by ISK 250 million.

Substantial uncertainty remains with regards to the impact of the COVID-19 pandemic on the credit quality of the Group’s credit exposures in future periods and therefore the assessment of expected credit losses.

The allowance for credit losses is further discussed in Notes 26-27, in Notes 47-55 on risk management and in Note 67.4.

Fair value of financial instruments

The fair value of financial instruments where an active market or quoted prices are not available are decided upon by using estimation procedures. Financial instruments measured at fair value are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. Level 3 financial assets are measured at fair value using valuation techniques based on significant unobservable inputs. The valuation of Level 3 financial assets is a subjective area as the assumption on which the valuation is based on is not easily observable and subject to management's assessment. Any changes made to the evaluation criteria could have a significant impact on the Group's results and financial position. The valuation methods are discussed in Notes 20-21 and in Note 67.4.

Intangible assets

Intangible assets are amortised over four to ten years. Intangible assets are reviewed at each reporting date to determine whether there is any indication of impairment. The value in use method is used by the Group to determine the recoverable amount of intangible assets. The following relevant criteria are considered when assessing whether indications of impairment exists:

- A decline in the asset's market value
- Plans to restructure or liquidate the asset
- The asset generates less income than anticipated

Intangible assets are further discussed in Note 30 and in Note 67.9.

Notes to the Consolidated Financial Statements

4. Changes to accounting policies

The Group adopted amendments to IAS 39 – Financial Instruments: Recognition and Measurement, and IFRS 7 – Financial Instruments: Disclosures (together referred to as "Interest Rate Benchmark Reform – Phase 1"), as of 1 January 2020. The amendments modified certain hedge accounting requirements, relating to the method that is used to assess the effectiveness of the hedging relationship, to provide relief from potential effect of uncertainty caused by the Interest Rate Benchmark Reform, prior to the transition to alternative benchmark interest rates. The amendments did not have a significant impact on the Group's consolidated financial statements.

To manage the transition to alternative benchmark interest rates the Bank has set up a working group responsible for the overall transition. A comprehensive review of legacy contracts has been carried out by the Bank's legal department and new contract language has been introduced to accommodate the benchmark reform. The work on systems and processes, along with education and communication to major stakeholders, is ongoing. It is expected that financial effects of the transition will be minimal to the Group. The Bank is continually monitoring developments in the benchmark reform work in jurisdictions affected and will adjust its implementation accordingly, should the need arise.

A number of other amendments to IFRS standards became effective from 1 January 2020 but they did not have a material impact on the Group's consolidated financial statements.

Changes to IFRS standards issued but not effective at the reporting date

A new IFRS standard and amendments to several IFRS standards have been issued but are not yet effective. The Group did not early adopt any of them and intends to adopt them when they become effective. Changes that are likely to affect the Group's future financial reporting are described below but no significant impact is currently expected.

Interest Rate Benchmark Reform - Phase 2

The Group adopted amendments to IFRS 9 – Financial Instruments, IAS 39 – Financial Instruments: Recognition and Measurement, IFRS 7 – Financial Instruments: Disclosures, and IFRS 16 – Leases (together referred to as "Interest Rate Benchmark Reform – Phase 2"), as of 1 January 2021. The amendments provide practical relief from certain requirements in the standards relating to the replacement of benchmark interest rates in contracts with new alternative benchmark interest rates. When the basis for determining the contractual cash flows of financial instruments is changed as a direct consequence of the Interest Rate Benchmark Reform and the change is made on an economically equivalent basis, the amendments provide a practical expedient to update the effective interest rate of the financial instruments rather than to recognise an immediate gain or loss in the income statement. The amendments also provide a series of reliefs from certain hedge accounting requirements when a change required by the Interest Rate Benchmark Reform occurs to a hedged item and/or hedging instrument. If qualifying criteria are met, hedging relationships that are directly impacted by the Interest Rate Benchmark Reform will be able to continue hedge accounting upon transition to alternative benchmark interest rates. The amendments will not have a significant impact on the Group's consolidated financial statements.

5. Investments in subsidiaries

		31.12.2020	31.12.2019
Íslandssjóðir hf., an investment fund management company, Hagasmári 3, 201 Kópavogur	Iceland	100%	100%
Allianz Ísland hf., an insurance agent, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%
Borgun hf., a payment acquirer and issuing processor, Ármúli 30, 108 Reykjavík	Iceland	-	63.5%

In addition Íslandsbanki has control over ten other non-significant subsidiaries.

Borgun hf.

A formal sale process of Borgun hf. began early in 2019, as was announced by Íslandsbanki on 11 January 2019. The sale was an open and transparent process led by Swiss based investment banking firm Corestar Partners and Íslandsbanki's Corporate Finance department.

On 11 March 2020 Íslandsbanki signed an agreement to sell its 63.5% stake in Borgun hf. to Salt Pay Co Ltd. but this transaction was subject to Financial Supervisory Authority of the Central Bank ("FSA") approval of the purchaser's acquisition of a qualifying holding. On 7 July 2020 the Bank concluded the sale. The net loss of Borgun hf. during the period, 1 January until the selling date 7 July 2020, amounting to ISK 828 million and net profit from the sale amounting to ISK 427 million is included in the line item "Discontinued operations, net of income tax" in the Consolidated Income Statement.

Before the sale, in the first quarter of 2020, Borgun hf. was classified as disposal group held for sale, in accordance with IFRS 5 - Non-current assets and disposal groups held for sale, resulting in a change in the presentation. As a result the comparative figures in the Consolidated Income Statement for the year 2019 have been restated and Borgun hf. is no longer presented separately in the Operating segments note.

Restated Consolidated Income Statement 2019	Published accounts	Reclassified Borgun hf.	Restated accounts
Interest income	62,846	(881)	61,965
Interest expense	(29,170)	27	(29,143)
Net interest income	33,676	(854)	32,822
Fee and commission income	21,026	(8,974)	12,052
Fee and commission expense	(7,667)	6,514	(1,153)
Net fee and commission income	13,359	(2,460)	10,899
Net financial income	(817)	(3)	(820)
Net foreign exchange loss	143	(4)	139
Other operating income	2,134	(9)	2,125
Other net operating income	1,460	(16)	1,444
Total operating income	48,495	(3,330)	45,165
Salaries and related expenses	(16,279)	2,260	(14,019)
Other operating expenses	(11,828)	1,359	(10,469)
Contribution to the Depositors' and Investors' Guarantee Fund	(936)	-	(936)
Bank tax	(3,528)	-	(3,528)
Total operating expenses	(32,571)	3,619	(28,952)
Profit before net impairment on financial assets	15,924	289	16,213
Net impairment on financial assets	(3,663)	183	(3,480)
Profit before tax	12,261	472	12,733
Income tax expense	(3,682)	(227)	(3,909)
Profit for the year from continuing operations	8,579	245	8,824
Discontinued operations, net of income tax	(125)	(245)	(370)
Profit for the year	8,454	-	8,454

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Notes to the Consolidated Financial Statements

5. Cont'd

The following tables summarise key information relevant to Borgun hf. The amounts shown are before inter-company eliminations.

Interim Income Statement of Borgun hf.	2020 1.1-7.7	2019 1.1-7.7
Net interest income	312	444
Net fee and commission income	800	768
Other operating income	(46)	39
Total operating income	1,066	1,251
Salaries and related expenses	(1,141)	(1,210)
Other operating expenses	(679)	(720)
Net impairment on financial assets	(84)	(39)
Loss before tax	(838)	(718)
Income tax expense	10	143
Loss for the period	(828)	(575)
Amounts included in other comprehensive income for the period		
Changes in fair value of financial assets, net of tax	(913)	893
Total comprehensive income (expense) for the period	(1,741)	318

Interim Statement of Financial Position of Borgun hf.	7.7.2020
Loans to credit institutions	7,123
Bonds and debt instruments	499
Derivatives	69
Loans to customers	4,309
Shares and equity instruments	3,559
Property and equipment	1,293
Intangible assets	445
Other assets	4,531
Total assets	21,828
Debt issued and other borrowed funds	266
Tax liabilities	21
Other liabilities	15,301
Total liabilities	15,588
Net assets of Borgun hf.	6,240

	2020 1.1-7.7	2019 1.1-7.7
Net cash used in operating activities	(512)	(2,952)
Net cash (used in) provided by investing activities	(923)	137
Net cash provided (used in) by financing activities	577	(403)
Net decrease in cash and cash equivalents	(858)	(3,218)

Íslandsbanki hf. Consolidated Financial Statements 2020 22 Amounts are in ISK million

6. Operating segments

Segment information is presented in accordance with the Group's management and internal reporting structure. The segments' operating result are reported to the Board of Directors and the Chief Executive Officer, who are responsible for allocating resources to the reportable segments and assessing their financial performance.

An operating segment is a distinguishable component of the Group, for which discrete financial information is available, that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. Each operating segment is engaged in providing products or services which are subject to risk and return that are different from those of other operating segments. The accounting policies for the reportable segments are in line with the Group's accounting policies. The Group operates mainly in the Icelandic market.

The Bank has three main business segments: Personal Banking, Business Banking and Corporate & Investment Banking. Operating segments pay and receive interest to and from Treasury to reflect the allocation of capital, funding costs and the relevant risk premium. Capital allocation to the business units is based on the pillar 1 regulatory capital requirement, the pillar 2-R capital requirement calculated according to the Bank’s ICAAP and the combined buffer requirement as stipulated in the act on financial undertakings. Income tax and bank tax with breakdown for each segment is according to the current tax rates.

The Group comprises the following operating segments:

Personal Banking

Personal Banking provides comprehensive financial services to individuals, such as lending, savings and payments. Íslandsbanki's customers are increasingly taking care of their day-to-day banking via digital solutions such as apps, the online bank and the secure web chat. Customers can also visit the Bank's efficient branch network for comprehensive consultancy services and contact the contact centre.

Business Banking

Business Banking provides small and medium-sized enterprises (SMEs) with comprehensive financial services and Ergo, the Bank's asset financing service, is also part of the division. Business Banking serves customers in business centres and branches close to their business. Via online banking and app, customers have full overview of their business and day-to-day operations are easy to manage.

Corporate & Investment Banking

Corporate & Investment Banking provides universal banking services to large companies, municipalities, institutional investors and affluent individuals. Services include customised products and services to customers including lending and advisory, risk management, brokerage and private banking services. The division is sector-focused, building and maintaining relationships with key customer segments within Iceland. Outside of Iceland, Íslandsbanki has a special focus on the North Atlantic seafood industry, leveraging its expertise in the domestic market and global contacts.

Treasury and Proprietary Trading

Treasury is responsible for funding the Bank's operations and for managing the internal pricing framework. It is also responsible for the Bank's balance sheet management and for relations with investors, financial institutions, stock exchanges and rating agencies. Equity that is not allocated to business units sits within Treasury. Proprietary Trading includes equity and debt investments in the trading book and banking book.

Cost centres

Cost centres comprise the CEO's office (Human Resources, Marketing & Communications, Strategy, and Legal), Finance excluding Treasury and Proprietary Trading, IT, Risk Management and Compliance. Group Internal Audit is included in cost centres, however, it is independent from the Bank and the Chief Audit Executive reports directly to the Bank's Board of Directors.

Subsidiaries, eliminations and adjustments

Subsidiaries include Íslandssjóðir hf., Allianz Ísland hf. and other less significant subsidiaries (see Note 5).

Before its sale on 7 July 2020, the subsidiary Borgun hf. was classified as non-current assets and disposal groups held for sale, accordingly the comparative figures in this disclosure have been restated.

Assets and liabilities of subsidiaries, that are classified as non-current assets and disposal groups held for sale, are included in the column “Other subsidiaries" and all inter-company eliminations for those subsidiaries are included in the column “Eliminations & adjustments".

Following is an overview showing the Group's performance with a breakdown by operating segments.

Notes to the Consolidated Financial Statements

6. Cont'd

2020	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	10,749	10,536	8,530	3,734	(215)	33,334	37	33,371
Net fee and commission income	3,049	1,917	4,075	(317)	7	8,731	1,794	10,525
Other net operating income	305	50	922	(1,420)	287	144	(887)	(743)
Total operating income	14,103	12,503	13,527	1,997	79	42,209	944	43,153
Salaries and related expenses	(2,416)	(1,940)	(1,583)	(280)	(5,926)	(12,145)	(772)	(12,917)
Other operating expenses	(2,584)	(1,164)	(870)	(263)	(4,488)	(9,369)	(460)	(9,829)
Contribution to the Depositors' and Investors' Guarantee Fund	(482)	(161)	(35)	(1)	-	(679)	-	(679)
Bank tax	(613)	(340)	(514)	(105)	(16)	(1,588)	-	(1,588)
Net impairment on financial assets	(517)	(5,485)	(2,805)	(8)	-	(8,815)	(1)	(8,816)
Cost allocation	(4,690)	(2,967)	(3,020)	323	10,354	-	-	-
Profit (loss) before tax	2,801	446	4,700	1,663	3	9,613	(289)	9,324
Income tax expense	(887)	(204)	(1,356)	112	(5)	(2,340)	(132)	(2,472)
Profit (loss) for the year from continuing operations	1,914	242	3,344	1,775	(2)	7,273	(421)	6,852
Net segment revenue from external customers	20,911	14,750	19,922	(13,597)	223	42,209	944	43,153
Net segment revenue from other segments	(6,808)	(2,247)	(6,395)	15,594	(144)	-	-	-
Fee and commission income	4,797	1,948	4,152	(9)	7	10,895	1,756	12,651
Depreciation, amortisation and write-offs	(300)	(163)	(18)	-	(1,178)	(1,659)	(7)	(1,666)
At 31 December 2020								
Loans to customers	419,882	232,580	353,953	302	-	1,006,717	-	1,006,717
Other assets	3,212	2,199	795	320,578	10,893	337,677	(203)	337,474
Total segment assets	423,094	234,779	354,748	320,880	10,893	1,344,394	(203)	1,344,191
Deposits from customers	324,815	189,847	137,791	31,674	-	684,127	(4,672)	679,455
Other liabilities	1,327	1,481	4,908	463,943	5,915	477,574	958	478,532
Total segment liabilities	326,142	191,328	142,699	495,617	5,915	1,161,701	(3,714)	1,157,987
Allocated equity	34,850	37,804	63,432	45,708	899	182,693	3,511	186,204
Risk exposure amount	229,610	235,371	392,804	60,037	5,960	923,782	9,739	933,521

The individual segment balance sheet positions are with external customers, and exclude internal transactions thus explaining the differences in total assets and total liabilities and equity.

Íslandsbanki hf. Consolidated Financial Statements 2020 24 Amounts are in ISK million

6. Cont'd

2019	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	10,578	10,812	8,397	3,169	(251)	32,705	117	32,822
Net fee and commission income	4,504	1,716	3,530	(236)	7	9,521	1,378	10,899
Other net operating income	77	25	564	(848)	2,197	2,015	(571)	1,444
Total operating income	15,159	12,553	12,491	2,085	1,953	44,241	924	45,165
Salaries and related expenses	(2,791)	(1,993)	(1,720)	(253)	(6,516)	(13,273)	(746)	(14,019)
Other operating expenses	(2,131)	(1,184)	(660)	(257)	(5,725)	(9,957)	(512)	(10,469)
Contribution to the Depositors' and Investors' Guarantee Fund	(530)	(314)	(89)	(3)	-	(936)	-	(936)
Bank tax	(483)	(339)	(486)	(2,205)	(15)	(3,528)	-	(3,528)
Net impairment on financial assets	(547)	(1,098)	(1,043)	(791)	-	(3,479)	(1)	(3,480)
Cost allocation	(5,606)	(3,381)	(3,421)	278	12,130	-	-	-
Profit (loss) before tax	3,071	4,244	5,072	(1,146)	1,827	13,068	(335)	12,733
Income tax expense	(924)	(1,192)	(1,445)	318	(478)	(3,721)	(188)	(3,909)
Profit (loss) for the year from continuing operations	2,147	3,052	3,627	(828)	1,349	9,347	(523)	8,824
Net segment revenue from external customers	18,137	14,492	19,191	(9,708)	2,129	44,241	924	45,165
Net segment revenue from other segments	(2,978)	(1,939)	(6,700)	11,793	(176)	-	-	-
Fee and commission income	6,224	1,724	3,574	124	8	11,654	398	12,052
Depreciation, amortisation and write-offs	(215)	(112)	(21)	-	(1,367)	(1,715)	(10)	(1,725)
At 31 December 2019								
Loans to customers	329,265	230,842	334,788	2	-	894,897	4,735	899,632
Other assets	3,553	3,085	347	267,384	10,648	285,017	14,841	299,858
Total segment assets	332,818	233,927	335,135	267,386	10,648	1,179,914	19,576	1,199,490
Deposits from customers	290,894	167,623	113,455	49,517	-	621,489	(3,176)	618,313
Other liabilities	1,497	1,822	2,553	374,459	6,209	386,540	14,575	401,115
Total segment liabilities	292,391	169,445	116,008	423,976	6,209	1,008,029	11,399	1,019,428
Allocated equity	29,981	38,924	58,953	42,882	1,145	171,885	8,177	180,062
Risk exposure amount	194,601	247,565	367,456	48,063	6,968	864,653	19,897	884,550

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Notes to the Consolidated Financial Statements

6. Cont'd

Subsidiaries, eliminations & adjustments

2020	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments*	Total
Net interest income	11	12	22	(8)	37
Net fee and commission income	1,185	724	(30)	(85)	1,794
Other net operating income	172	10	9	(1,078)	(887)
Total operating income	1,368	746	1	(1,171)	944
Salaries and related expenses	(584)	(188)	-	-	(772)
Other operating expenses	(183)	(420)	(1)	144	(460)
Net impairment on financial assets	-	-	-	(1)	(1)
Profit (loss) before tax	601	138	-	(1,028)	(289)
Income tax expense	(119)	(11)	-	(2)	(132)
Profit (loss) for the year from cont. operations	482	127	-	(1,030)	(421)
Net segment revenue from external customers	1,651	646	-	(1,353)	944
Net segment revenue from other segments	(283)	100	1	182	-
Fee and commission income	1,664	725	-	(633)	1,756
Depreciation, amortisation and write-offs	-	8	-	(15)	(7)
At 31 December 2020					
Total assets	2,249	1,425	9,080	(12,957)	(203)
Total liabilities	271	600	36	(4,621)	(3,714)
Total equity	1,978	825	9,044	(8,336)	3,511

*Included are all eliminations on consolidation and the impact of the sale of Borgun hf.

2019	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments	Total
Net interest income	28	26	36	27	117
Net fee and commission income	1,089	1,069	(30)	(750)	1,378
Other net operating income	156	(1)	(5)	(721)	(571)
Total operating income	1,273	1,094	1	(1,444)	924
Salaries and related expenses	(558)	(188)	-	-	(746)
Other operating expenses	(181)	(471)	(2)	142	(512)
Net impairment on financial assets	-	-	-	(1)	(1)
Profit (loss) before tax	534	435	(1)	(1,303)	(335)
Income tax expense	(107)	(87)	-	6	(188)
Profit (loss) for the year from cont. operations	427	348	(1)	(1,297)	(523)
Net segment revenue from external customers	1,475	1,080	(16)	(1,615)	924
Net segment revenue from other segments	(202)	14	17	171	-
Fee and commission income	1,520	1,069	-	(2,191)	398
Depreciation, amortisation and write-offs	-	(3)	-	(7)	(10)
At 31 December 2019					
Total assets	2,726	1,201	28,829	(13,180)	19,576
Total liabilities	302	412	15,755	(5,070)	11,399
Total equity	2,424	789	13,074	(8,110)	8,177

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Notes to the Consolidated Financial Statements

7. Quarterly statements (unaudited)

2020	Q4	Q3	Q2	Q1	Total
Net interest income	8,258	8,305	8,228	8,580	33,371
Net fee and commission income	2,865	2,862	2,307	2,491	10,525
Net financial income (expense)	783	(255)	(181)	(1,738)	(1,391)
Net foreign exchange gain	87	101	208	55	451
Other operating income	63	44	71	19	197
Salaries and related expenses	(3,381)	(2,842)	(3,447)	(3,247)	(12,917)
Other operating expenses	(2,692)	(2,268)	(2,424)	(2,445)	(9,829)
Contribution to the Depositors' and Investors' Guarantee Fund	(154)	(50)	(247)	(228)	(679)
Bank tax	(414)	(416)	(399)	(359)	(1,588)
Net impairment on financial assets	(1,829)	(1,058)	(2,439)	(3,490)	(8,816)
Profit (loss) before tax	3,586	4,423	1,677	(362)	9,324
Income tax expense	(234)	(1,350)	(119)	(769)	(2,472)
Profit (loss) for the period from continuing operations	3,352	3,073	1,558	(1,131)	6,852
Discontinued operations, net of income tax	173	288	(313)	(245)	(97)
Profit (loss) for the period	3,525	3,361	1,245	(1,376)	6,755

8. Net interest income

	2020	2019
Cash and balances with Central Bank	1,750	4,452
Loans at amortised cost	51,628	54,837
Financial assets mandatorily at fair value through profit or loss	2,314	2,630
Other assets	3	46
Total interest income	55,695	61,965
Deposits from Central Bank and credit institutions	(736)	(625)
Deposits from customers	(7,700)	(15,242)
Debt issued and other borrowed funds at fair value through profit or loss	(608)	(734)
Debt issued and other borrowed funds at amortised cost	(11,179)	(9,818)
Subordinated loans	(763)	(501)
Other interest expense*	(1,338)	(2,223)
Total interest expense	(22,324)	(29,143)
Net interest income	33,371	32,822

*Thereof is lease liabilities' interest expense amounting to ISK 87 million (2019: ISK 70 million).
Net interest margin on total assets 2.6% (2019: 2.7%).

9. Net fee and commission income

	2020	2019
Asset management	2,382	2,225
Investment banking and brokerage	2,487	2,430
Payment processing	4,378	3,810
Loans and guarantees	2,014	1,510
Other fee and commission income	1,390	2,077
Total fee and commission income	12,651	12,052

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9. Cont'd

	2020	2019
Brokerage	(360)	(337)
Clearing and settlement	(1,766)	(806)
Other fee and commission expense	-	(10)
Total fee and commission expense	(2,126)	(1,153)
Net fee and commission income	10,525	10,899

Fee and commission income by segment is disclosed in Note 6.

10. Net financial expense

	2020	2019
Net loss on financial assets and financial liabilities mandatorily at FVTPL	(1,321)	(422)
Net loss on financial liabilities designated as at FVTPL	(72)	(399)
Net gain on fair value hedges	2	1
Net financial expense	(1,391)	(820)
Shares and related derivatives	165	(575)
Dividend income	18	32
Bonds and related derivatives	(1,586)	144
Other derivatives	82	(23)
Net loss on financial assets and financial liabilities mandatorily at FVTPL	(1,321)	(422)
Debt issued and other borrowed funds designated as at FVTPL	(72)	(399)
Net loss on financial liabilities designated as at FVTPL	(72)	(399)
Clean fair value gain on interest rate swaps designated as hedging instruments	54	285
Fair value loss on bonds issued by the Group attributable to interest rate risk	(52)	(284)
Net gain on fair value hedges	2	1

11. Net foreign exchange gain

	2020	2019
Cash and balances with Central Bank	160	(222)
Financial assets mandatorily at fair value through profit or loss	13,652	(1,781)
Loans at amortised cost	22,673	5,686
Other assets	10	-
Net foreign exchange gain for assets	36,495	3,683
Deposits	(10,279)	(1,749)
Debt issued and other borrowed funds designated as at FVTPL	(6,468)	(1,667)
Debt issued and other borrowed funds at amortised cost	(14,802)	(362)
Subordinated loans	(4,495)	234
Net foreign exchange loss for liabilities	(36,044)	(3,544)
Net foreign exchange gain	451	139

Íslandsbanki hf. Consolidated Financial Statements 2020 28 Amounts are in ISK million

12. Other operating income

	2020	2019
Share of profit of associates, net of income tax	44	63
Legal dispute settlement	-	1,103
Legal fees	90	93
Rental income	39	38
Depositor's and Investor's Guarantee Fund reversed contribution	-	847
Other net operating income (expense)	24	(19)
Other operating income	197	2,125

13. Personnel and salaries

	2020	2019
Salaries	9,940	10,801
Contributions to pension funds	1,505	1,618
Social security charges and financial activities tax*	1,391	1,493
Other salary-related expenses	81	107
Salaries and related expenses	12,917	14,019

*Financial activities tax calculated on salaries is 5.5% (2019: 5.5%).

	2020		2019	
	The Bank	The Group	The Bank	The Group
Average number of employees	774	910	842	1,079
Positions at year-end	745	779	749	984

Total amount of compensation to the Board of Directors, the CEO and Executive Board are specified as follows:

	2020	2019
Hallgrímur Snorrason, Chairman of the Board	10.5	7.6
Heiðrún Jónsdóttir, Vice-Chairman of the Board	8.9	7.9
Anna Þórðardóttir, member of the Board	7.9	7.9
Árni Stefánsson, member of the Board	7.9	7.8
Frosti Ólafsson, member of the Board	5.9	-
Guðrún Þorgeirsdóttir, member of the Board	5.9	-
Herdís Gunnarsdóttir, member of the Board	0.4	-
Friðrik Sophusson, former Chairman of the Board	2.5	11.3
Tómas Már Sigurðsson, former Vice-Chairman of the Board	2.0	6.6
Auður Finnbogadóttir, former member of the Board	1.7	7.6
Flóki Halldórsson, former member of the Board	4.7	-
Helga Valfells, former Vice-Chairman of the Board	-	2.3
Alternate board members	-	1.3
Total salaries	58.3	60.3

Contribution to pension funds for the Board of Directors amounted to ISK 8.8 million (2019: ISK 7.1 million).

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Notes to the Consolidated Financial Statements

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	2020		2019	
	Total salaries	Contri- butions to pension funds	Total salaries	Contri- butions to pension funds
Birna Einarsdóttir, CEO	48.7	11.6	50.9	11.9
Ásmundur Tryggvason, Managing Director of Corporate & Investment Banking	43.3	6.1	39.5	5.6
Guðmundur Kristinn Birgisson, Chief Risk Officer	36.5	5.2	36.1	5.1
Jón Guðni Ómarsson, Chief Financial Officer	42.0	5.9	41.5	6.1
Riaan Dreyer, Director of Information Technology	37.7	5.6	13.6	2.0
Sigríður Hrefna Hrafnkelsdóttir, Managing Director of Personal Banking	37.7	5.3	37.8	5.3
Una Steinsdóttir, Managing Director of Business Banking*	50.8	7.4	42.6	6.1
Sigríður Olgeirsdóttir, former Director of Information Technology	-	-	22.8	3.3
Vilhelm Þorsteinsson, former Managing Director of Corporate & Investment Banking	-	-	3.3	0.5
Total	296.7	47.1	288.1	45.9

*The salary increase is due to an employment anniversary payment for 30 years of service. The payment is in accordance with the collective agreement of the Confederation of Icelandic Bank and Finance Employees (SSF).

The amounts in the table above comprise salaries for the managing directors for their executive board responsibilities. Included in total salaries are non-monetary benefits such as the use of cars owned by the Group.

As of 1 January 2017, the Bank has not had an active remuneration policy in place as stated in the Bank's compensation policy. Included in total salaries are paid performance-based salaries, which were earned in 2016, and paid by the Bank in 2020. For the Bank's CEO those amounted to ISK 3.9 million (2019: ISK 4.1 million) and for the managing directors the payments amounted to ISK 8.8 million (2019: ISK 10.7 million). There were no unpaid performance-based salaries at year-end 2020.

There were no share based payments in the years 2020 and 2019.

14. Other operating expenses

	2020	2019
Professional services	1,539	1,778
Software and IT expenses	4,581	4,616
Real estate and office equipment	627	593
Depreciation, amortisation and write-offs	1,666	1,725
Other administrative expenses	1,416	1,757
Other operating expenses	9,829	10,469

Auditors' fees

	2020	2019
Audit of the financial statements	92	99
Review of interim financial statements	18	16
Other services	6	5
Auditors' fees	116	120

15. Net impairment on financial assets

	2020	2019
Expected credit loss, on-balance sheet items*	(8,450)	(3,341)
Expected credit loss, off-balance sheet items	(366)	(52)
Changes in provision due to court rulings	-	(87)
Net impairment on financial assets	(8,816)	(3,480)

*The main reasons for the additional expected credit loss allowance are: an increase related to the COVID-19 pandemic (ISK 6,115 million), increased expected credit loss for a few customers (ISK 1,185 million), and due to a less favourable economic environment (ISK 583 million). For further information see Note 3.

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16. Income tax expense

Recognised income tax is based on applicable tax laws. The income tax rate for legal entities in 2020 is 20% (2019: 20%). Special financial activities tax is calculated as 6% of taxable profit exceeding ISK 1 billion in accordance with the Act on Financial Activities Tax no. 165/2011. The special financial activities tax is calculated on the Bank's profit. The effective income tax rate in the Group's income statement for the year 2020 is 26.5% (2019: 30.7%).

	2020	2019
Current tax expense excluding discontinued operations	3,052	2,610
Special financial activities tax	801	642
Difference in prior year's calculated income tax	68	(1)
Changes in deferred tax assets and deferred tax liabilities	(1,449)	658
Income tax recognised in the income statement	2,472	3,909

Income tax recognised in other comprehensive income	(16)	(233)

	2020		2019	
Profit before tax	9,324		12,733	
20% income tax calculated on the profit for the year	1,865	20.0%	2,547	20.0%
Special financial activities tax	801	8.6%	642	5.0%
Income not subject to tax	(566)	(6.1%)	(143)	(1.1%)
Non-deductible expenses	318	3.4%	708	5.6%
Other differences	54	0.6%	155	1.2%
Effective income tax expense	2,472	26.5%	3,909	30.7%

The Bank is taxed jointly with its subsidiary Íslandssjóðir hf.

17. Discontinued operations, net of income tax

	2020	2019
Net profit (loss) from foreclosed assets	37	(178)
Net loss from disposal groups held for sale	(542)	(171)
Net profit from sale of a subsidiary	427	-
Income tax expense	(19)	(21)
Discontinued operations, net of income tax	(97)	(370)

18. Earnings per share

	Discontinued operations			
	Excluded		Included	
	2020	2019	2020	2019
Profit attributable to shareholders of the Bank	7,158	9,179	7,061	8,809
Weighted average number of outstanding shares	10,000	10,000	10,000	10,000
Basic earnings per share	0.72	0.92	0.71	0.88

The Group's basic and diluted earnings per share are equal as the Group has not issued any options, warrants, convertibles, or other financial instruments that dilute earnings per share (2019: none).

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19. Classification of financial assets and financial liabilities

At 31 December 2020	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	78,948	78,948
Loans to credit institutions	-	-	-	89,920	89,920
Listed bonds and debt instruments	90,603	-	-	-	90,603
Listed bonds and debt instruments used for economic hedging	37,468	-	-	-	37,468
Unlisted bonds and debt instruments	145	-	-	-	145
Derivatives	5,639	1,008	-	-	6,647
Loans to customers	-	-	-	1,006,717	1,006,717
Listed shares and equity instruments	2,933	-	-	-	2,933
Listed shares and equity instruments used for economic hedging	9,109	-	-	-	9,109
Unlisted shares and equity instruments	2,809	-	-	-	2,809
Other financial assets	-	-	-	3,692	3,692
Total financial assets	148,706	1,008	-	1,179,277	1,328,991
Deposits from Central Bank and credit institutions	-	-	-	39,758	39,758
Deposits from customers	-	-	-	679,455	679,455
Derivative instruments and short positions	6,936	-	-	-	6,936
Debt issued and other borrowed funds	-	48,032	94,438	244,804	387,274
Subordinated loans	-	-	-	27,194	27,194
Other financial liabilities	-	-	-	9,721	9,721
Total financial liabilities	6,936	48,032	94,438	1,000,932	1,150,338

At 31 December 2019	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Fair value through OCI	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	-	146,638	146,638
Loans to credit institutions	-	-	-	-	54,376	54,376
Listed bonds and debt instruments	33,302	-	-	-	-	33,302
Listed bonds and debt instruments used for economic hedging	18,220	-	-	-	-	18,220
Unlisted bonds and debt instruments	1,348	-	-	-	-	1,348
Derivatives	4,700	921	-	-	-	5,621
Loans to customers	-	-	-	-	899,632	899,632
Listed shares and equity instruments	3,779	-	-	-	-	3,779
Listed shares and equity instruments used for economic hedging	8,681	-	-	-	-	8,681
Unlisted shares and equity instruments	2,851	-	-	3,115	-	5,966
Other financial assets	-	-	-	-	5,757	5,757
Total financial assets	72,881	921	-	3,115	1,106,403	1,183,320
Deposits from Central Bank and credit institutions	-	-	-	-	30,925	30,925
Deposits from customers	-	-	-	-	618,313	618,313
Derivative instruments and short positions	6,219	-	-	-	-	6,219
Debt issued and other borrowed funds	-	41,816	49,352	-	215,213	306,381
Subordinated loans	-	-	-	-	22,674	22,674
Other financial liabilities	-	-	-	-	24,772	24,772
Total financial liabilities	6,219	41,816	49,352	-	911,897	1,009,284

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20. Fair value information for financial instruments

Financial instruments carried at fair value

The fair value of a financial instrument is the transaction price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where a market price is not readily available, the Group applies valuation techniques based on estimates and assumptions that are consistent with that which market participants would use in setting a price for the financial instrument.

The table below shows financial instruments carried at fair value at 31 December 2020 categorised into three levels of fair value hierarchy that reflect the type of inputs used in making the fair value measurements. The different levels have been defined as follows:

Level 1: Inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Group can access at the measurement date.

Level 2: Valuation techniques based on observable inputs other than the quoted prices included in Level 1, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Valuation techniques based on significant unobservable inputs, e.g. internal assumptions.

At 31 December 2020	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	128,071	-	145	128,216
Derivatives	-	6,647	-	6,647
Shares and equity instruments	11,931	30	2,890	14,851
Non-current assets and disposal groups held for sale	-	-	1,266	1,266
Total financial assets	140,002	6,677	4,301	150,980
Short positions	737	-	-	737
Derivative instruments	-	6,199	-	6,199
Debt issued and other borrowed funds designated as at FVTPL	94,438	-	-	94,438
Total financial liabilities	95,175	6,199	-	101,374

At 31 December 2019	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	51,522	-	1,348	52,870
Derivatives	-	5,621	-	5,621
Shares and equity instruments	12,383	27	6,016	18,426
Total financial assets	63,905	5,648	7,364	76,917
Short positions	814	-	-	814
Derivative instruments	-	5,405	-	5,405
Debt issued and other borrowed funds designated as at FVTPL	49,352	-	-	49,352
Total financial liabilities	50,166	5,405	-	55,571

Changes in Level 3 assets measured at fair value	Bonds and debt instruments	Shares and equity instruments	Non-current assets
Fair value at 1 January 2020	1,348	6,016	-
Purchases	18	7	-
Sales	-	-	(2,028)
Net loss on financial instruments recognised in profit or loss	(1,256)	(2)	-
Net gain on financial instruments recognised in other comprehensive income	-	-	114
Transfer to "Non-current assets and disposal groups held for sale"	-	(3,180)	3,180
Other changes	35	49	-
Fair value at 31 December 2020	145	2,890	1,266

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	Bonds and debt instruments	Shares and equity instruments
Fair value at 1 January 2019	1,514	4,688
Purchases	7	338
Sales and instalments	(537)	(52)
Net gain (loss) on financial instruments recognised in profit or loss	306	(118)
Net gain on financial instruments recognised in other comprehensive income	-	1,272
Other changes	58	(112)
Fair value at 31 December 2019	1,348	6,016

At the end of each reporting period the Group determines whether transfers have occured between levels in the hierarchy, by reassessing categorisation based on the lowest level input that is significant to the fair value measurement as a whole. No transfers between levels took place during the year.

Valuation process

The responsibility for the valuation of the fair value of financial instruments lies with the relevant business units. Each quarter, the business units present a valuation report to the Investment Committee for approval. The report and its assumptions are reviewed by Risk Management.

Valuation techniques

Where applicable, fair values are determined using quoted prices in active markets for identical assets and liabilities. In other cases, where there is no active market, the fair value is estimated using valuation techniques such as net present value and discounted cash flow models; comparison with similar instruments for which observable market data exists; net asset value (NAV) for investment fund units or expected recovery for distressed bonds. These valuation techniques are based on various assumptions and inputs such as risk-free rate, expected revenue growth and credit and liquidity spreads. In some cases, where significant inputs into these models are not observable, expert judgement and estimation for these inputs are required.

Level 1: Fair value established from quoted market prices.

Assets at this level are financial assets and financial liabilities containing actively traded bonds and equities that are listed either domestically or abroad.

Level 2: Fair value established using valuation techniques with observable market information.

Assets at this level are assets and liabilities containing domestic bonds, equities as well as derivatives. For interest rate derivatives contracts such as interest rate swaps (IRS) and cross-currency interest rate swaps (CIRS) the Group calculates the net present value of estimated future cash flows based on yield curves with key inputs such as interest swap rates and forward-rate agreements (FRAs) rates. Foreign-currency forwards and foreign-currency swaps are valued using the FX spot rate adjusted for forward pricing points that can be obtained from market sources. These products are classified as Level 2. Bond forwards and equity forwards are also classified as Level 2 as they are valued using standard models with key inputs observed from stock prices, estimated dividend rates and funding rates.

Level 3: Fair value established using valuation techniques using significant unobservable market information.

Assets at this level contain primarily unlisted and illiquid equities and bonds. Unlisted equities and bonds are initially recorded at their transaction price but are revalued each quarter based on the models as described above.

The economic crisis relating to the COVID-19 pandemic is the main reason for the decrease in Level 3 bonds and debt instruments during the year.

At 31 December 2020 the Group's Level 3 equities amounted to ISK 2,890 million:

-These include shares in seven professional investment funds and investment companies investing in unlisted equities and specialised investments in Iceland totalling ISK 1,676 million. The Group receives information from fund managers which use valuation models for the valuation of these equities.

-Other Level 3 equities amounting to ISK 1,214 million.

-Series C preferred shares in Visa Inc., which the Group holds, were reclassified as held for sale during the year and transfered to "Non-current assets and disposal groups held for sale".

At 31 December 2020 the Group's Level 3 bonds amounted to ISK 145 million:

-The majority of the amount in Level 3 bonds is estimated by discounting cash flow where the yield is the contractual currency's base rate with a premium that is decided by expert judgement on projected risk and financing cost.

At 31 December 2020 the Group's Level 3 shares classified as an asset held for sale in the consolidated financial statements amounted to ISK 1,266 million:

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The Group holds Series C preferred shares in Visa Inc. amounting to ISK 1,266 million, which are subject to selling restrictions for a period of up to eight years. Shares in this series will be converted into Series A shares listed on the New York Stock Exchange (NYSE), but the number of shares that the Group will receive in that series will be determined by the share price of the class as well as the amount of compensation that Visa Inc. may have to pay in connection with certain disputes brought before courts in several European countries. The fair value of the preferred shares is therefore determined by the market value of Visa Inc. in addition to an assessment of the present value of possible claims for damages. It is clear that important factors in the fair value calculation are based on a subjective assessment.

Sensitivity analysis for Level 3 assets

The valuations of Level 3 assets are in general uncertain and subject to various factors. The favourable and unfavourable scenarios can be considered as being likely movements in valuation within a year. The very favourable and very unfavourable scenarios are considered less likely, but not impossible and are not worst-case scenarios for some of the assets.

The table below shows how profit (loss) and total comprehensive income would have been affected if one or more of the inputs for fair value measurement in Level 3 were changed.

At 31 December 2020					
Effect on profit or (loss):	Carrying amount	Very favourable	Favourable	Unfavourable	Very unfavour-able
Level 3 Bonds and debt instruments	145	1,015	773	(132)	(145)
Level 3 Shares and equity instruments	2,890	1,897	539	(571)	(878)
Effect on comprehensive income:					
Level 3 Non-current assets and disposal groups held for sale	1,266	1,898	949	(633)	(1,266)

At 31 December 2019					
Effect on profit or (loss):	Carrying amount	Very favourable	Favourable	Unfavourable	Very unfavour-able
Level 3 Bonds and debt instruments	1,348	330	257	(296)	(1,348)
Level 3 Shares and equity instruments	2,901	2,399	645	(762)	(1,614)
Effect on comprehensive income:					
Level 3 Shares in Visa Inc.	3,115	1,246	623	(623)	(1,246)

21. Financial instruments not carried at fair value

Assets

The fair value of “Loans to customers” may differ from their net carrying amount because the interest rates they carry may not reflect the interest rates that similar new loans would carry. The fair value is estimated by subtracting from or adding to the net carrying amount of the loans the discounted interest rate difference calculated from the reporting date until the next interest reset or maturity, whichever comes first. Since the interest rate difference is estimated using internal models these assets are classified as Level 3.

For “Cash and balances with Central Bank”, “Loans to credit institutions” and “Other financial assets” the fair value is adequately approximated by the carrying amount as they are short-term in nature. They are thus classified as Level 2.

Liabilities

The fair value of a financial liability with a demand feature, such as a demand deposit, is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid. Most deposits are on demand or carry floating interest rates and as such their carrying amount is considered a good approximation of their fair value. The fair value for longer term fixed rate deposits is calculated with a duration approach, using the difference in each liability's current interest rate from the rate that a similar deposit would carry today. All deposits are classified as Level 2 based on the use of observable market interest rates to estimate the fair value.

Observed market value is used for the fair value of "Debt issued and other borrowed funds" where it is available. Issued bonds and bills with quoted market prices are classified as Level 1. If there is no quoted market price the fair value of the debt is valued in the same manner as deposits if it carries a fixed rate. If the debt carries a floating rate its fair value is estimated by comparing the margin with the Group's current funding premium on similar debt. These liabilities are classified as Level 2. The funding premium is based on the interest margin in the Group's issued papers including covered bonds, commercial papers as well as foreign currency denominated bonds.

Other financial liabilities mainly include unsettled securities transactions and payments due to leasing contracts and they are classified as Level 2 since their value is not observable from active market prices. Due to the short-term nature of these liabilities their carrying amount is considered a good approximation of their fair value.

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The following table shows the fair value measurement and classification of the Group's assets and liabilities not carried at fair value. The different levels are defined in Note 20.

At 31 December 2020	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	78,948	-	78,948	78,948
Loans to credit institutions	-	89,920	-	89,920	89,920
Loans to customers	-	-	1,010,315	1,010,315	1,006,717
Other financial assets	-	3,692	-	3,692	3,692
Total financial assets	-	172,560	1,010,315	1,182,875	1,179,277
Deposits from Central Bank and credit institutions	-	39,827	-	39,827	39,758
Deposits from customers	-	679,607	-	679,607	679,455
Debt issued and other borrowed funds	194,849	112,165	-	307,014	292,836
Subordinated loans	-	26,003	-	26,003	27,194
Other financial liabilities	-	9,721	-	9,721	9,721
Total financial liabilities	194,849	867,323	-	1,062,172	1,048,964

At 31 December 2019	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	146,638	-	146,638	146,638
Loans to credit institutions	-	54,376	-	54,376	54,376
Loans to customers	-	-	902,053	902,053	899,632
Other financial assets	-	5,757	-	5,757	5,757
Total financial assets	-	206,771	902,053	1,108,824	1,106,403
Deposits from Central Bank and credit institutions	-	31,027	-	31,027	30,925
Deposits from customers	-	618,592	-	618,592	618,313
Debt issued and other borrowed funds	165,044	100,334	-	265,378	257,029
Subordinated loans	22,626	-	-	22,626	22,674
Other financial liabilities	-	24,772	-	24,772	24,772
Total financial liabilities	187,670	774,725	-	962,395	953,713

22. Offsetting financial assets and financial liabilities

The following tables show reconciliation to the net amounts of financial assets and financial liabilities, which are subject to offsetting, enforceable master netting agreements and similar agreements.

	Financial assets subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 31 December 2020	Financial assets before netting	Netting with financial liabilities	Net financial assets	Financial liabilities	Cash collateral received	Financial instruments collateral received	Net amount after consideration of potential effect of netting arrangements	Assets outside the scope of offsetting disclosure requirements	Total financial assets recognised in the balance sheet
Reverse repurchase agreements ..	898	-	898	-	-	-	898	-	898
Derivatives	6,647	-	6,647	(761)	(4,330)	(187)	1,369	-	6,647
Total assets	7,545	-	7,545	(761)	(4,330)	(187)	2,267	-	7,545

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At 31 December 2019	Financial assets subject to netting arrangements: Financial assets before netting	Netting with financial liabilities	Net financial assets	Amounts not set off but subject to master netting arrangements and similar agreements: Financial liabilities	Cash collateral received	Financial instruments collateral received	Net amount after consideration of potential effect of netting arrangements	Assets outside the scope of offsetting disclosure requirements	Total financial assets recognised in the balance sheet
Reverse repurchase agreements ..	1,114	-	1,114	-	-	-	1,114	-	1,114
Derivatives	5,621	-	5,621	(1,374)	(3,146)	(88)	1,013	-	5,621
Total assets	6,735	-	6,735	(1,374)	(3,146)	(88)	2,127	-	6,735

	Financial liabilities subject to netting arrangements: Financial liabilities before netting	Netting with financial assets	Net financial liabilities	Amounts not set off but subject to master netting arrangements and similar agreements: Financial assets	Cash collateral pledged	Financial instruments collateral pledged	Net amount after consideration of potential effect of netting arrangements	Liabilities outside the scope of offsetting disclosure requirements	Total financial liabilities recognised in the balance sheet
At 31 December 2020									
Derivative instruments and short positions	6,936	-	6,936	(761)	(504)	-	5,671	-	6,936
At 31 December 2019									
Derivative instruments and short positions	6,219	-	6,219	(1,374)	(1,139)	-	3,706	-	6,219

23. Cash and balances with Central Bank

	31.12.2020	31.12.2019
Cash on hand	3,814	4,403
Balances with Central Bank	65,585	125,842
Balances with Central Bank subject to special restrictions*	1,288	1,679
Included in cash and cash equivalents	70,687	131,924
Cash and balances pledged as collateral to the Central Bank	288	1,114
Mandatory reserve deposits with Central Bank	7,973	13,600
Cash and balances with Central Bank	78,948	146,638

*Balances as defined in Act no. 37/2016 on the treatment of króna-denominated assets subject to special restrictions and rules no. 490/2016 on special reserve requirements for new foreign currency inflows.

24. Loans to credit institutions

	31.12.2020	31.12.2019
Money market loans	43,646	33,254
Bank accounts	46,269	21,122
Other loans	5	-
Loans to credit institutions	89,920	54,376

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25. Derivative instruments and short positions

At 31 December 2020	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	1,888	181,914	3,581	62,275
Cross-currency interest rate swaps	2,861	63,067	45	3,171
Equity forwards	7	813	1,488	6,702
Foreign exchange forwards	70	4,010	362	8,582
Foreign exchange swaps	1,738	32,227	435	24,101
Foreign exchange options	-	-	1	25
Bond forwards	83	10,907	287	29,596
Derivatives	6,647	292,938	6,199	134,452
Short positions in listed bonds	-	-	737	550
Total	6,647	292,938	6,936	135,002

At 31 December 2019	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	1,254	114,393	3,575	96,212
Cross-currency interest rate swaps	3,015	91,950	880	13,073
Equity forwards	141	4,664	298	4,001
Foreign exchange forwards	212	5,460	321	10,217
Foreign exchange swaps	867	30,990	298	24,928
Bond forwards	132	12,756	33	6,219
Derivatives	5,621	260,213	5,405	154,650
Short positions in listed bonds	-	-	814	734
Total	5,621	260,213	6,219	155,384

The Group uses derivatives to hedge currency exposure, interest rate risk in the banking book as well as inflation risk. The Group carries relatively low indirect exposure due to margin trading with clients and the Group holds collaterals for possible losses. Other derivatives in the Group held for trading or for other purposes are insignificant.

Short positions are in Icelandic Government bonds and bonds issued by municipalities, banks and public companies. As a primary dealer the Group has access to securities lending facilities provided by the Central Bank and other issuers. Majority of the securities lending facilities have a maturity of less than a year.

The Group applies hedge accounting only with respect to certain EUR denominated interest rate swaps, whereby the Group pays floating rate interest and receives fixed rate interest. The interest rate swaps are hedging the exposure of changes in the fair value of certain fixed-rate EUR denominated bonds (see Note 36) arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 31 December 2020 the total fair value of the interest rate swaps was positive and amounted to ISK 1,008 million (2019: ISK 921 million) and their total notional amount was ISK 46,830 million (2019: ISK 40,749).

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26. Loans to customers

At 31 December 2020	Gross carrying amount Stage 1	Stage 2	Stage 3	Expected credit loss Stage 1	Stage 2	Stage 3	Net carrying amount
Individuals	423,570	9,011	7,561	(1,608)	(254)	(903)	437,377
Commerce and services	60,062	64,350	5,958	(511)	(3,151)	(2,448)	124,260
Construction	36,551	5,420	997	(283)	(195)	(138)	42,352
Energy	7,997	701	-	(17)	(8)	-	8,673
Financial services	1,539	-	-	-	-	-	1,539
Industrial and transportation	46,526	30,971	3,989	(243)	(783)	(1,899)	78,561
Investment companies	15,287	5,504	3,628	(268)	(427)	(284)	23,440
Public sector and non-profit organisations	10,869	58	1	(17)	-	-	10,911
Real estate	112,189	42,169	6,794	(461)	(1,655)	(1,534)	157,502
Seafood	120,845	1,365	319	(237)	(9)	(181)	122,102
Loans to customers	835,435	159,549	29,247	(3,645)	(6,482)	(7,387)	1,006,717

At 31 December 2019	Gross carrying amount Stage 1	Stage 2	Stage 3	Expected credit loss Stage 1	Stage 2	Stage 3	Net carrying amount
Individuals	338,335	4,119	9,362	(1,319)	(168)	(1,148)	349,181
Commerce and services	115,679	6,999	6,515	(739)	(194)	(1,772)	126,488
Construction	39,248	849	4,924	(310)	(53)	(238)	44,420
Energy	7,913	-	-	(26)	-	-	7,887
Financial services	2,315	-	-	-	-	-	2,315
Industrial and transportation	77,492	3,338	3,503	(278)	(221)	(1,546)	82,288
Investment companies	19,542	4,369	265	(260)	(216)	(110)	23,590
Public sector and non-profit organisations	12,279	44	15	(23)	(2)	(1)	12,312
Real estate	140,604	3,831	2,345	(542)	(89)	(590)	145,559
Seafood	105,411	249	385	(148)	(10)	(295)	105,592
Loans to customers	858,818	23,798	27,314	(3,645)	(953)	(5,700)	899,632

27. Expected credit loss

Total allowances for expected credit losses

	Stage 1	Stage 2	Stage 3	Total
Cash and balances with Central Bank	2	-	-	2
Loans to credit institutions	109	-	-	109
Loans to customers	3,645	6,482	7,387	17,514
Other financial assets	15	4	-	19
Off-balance sheet loan commitments and financial guarantees	347	483	225	1,055
At 31 December 2020	4,118	6,969	7,612	18,699
Cash and balances with Central Bank	4	-	-	4
Loans to credit institutions	67	-	-	67
Loans to customers	3,645	953	5,700	10,298
Other financial assets	9	3	86	98
Off-balance sheet loan commitments and financial guarantees	403	55	231	689
At 31 December 2019	4,128	1,011	6,017	11,156

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The following tables reconcile the opening and closing balances for accumulated expected credit losses for loans to customers, and off-balance sheet loan commitments and financial guarantees.

Loans to customers

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	3,645	953	5,700	10,298
Transfer to Stage 1	3,577	(2,827)	(750)	-
Transfer to Stage 2	(1,743)	3,200	(1,457)	-
Transfer to Stage 3	(171)	(1,314)	1,485	-
Transfer to "Non-current assets and disposal groups held for sale"	(50)	(12)	(83)	(145)
Net remeasurement of loss allowance	(3,316)	6,024	1,201	3,909
New financial assets originated or purchased	2,104	597	2,516	5,217
Derecognitions and maturities	(401)	(139)	(404)	(944)
Write-offs	-	-	(1,498)	(1,498)
Recoveries of amounts previously written off	-	-	159	159
Foreign exchange	-	-	37	37
Unwinding of interest	-	-	481	481
At 31 December 2020	3,645	6,482	7,387	17,514
At 1 January 2019	3,277	1,079	3,689	8,045
Transfer to Stage 1	1,725	(1,343)	(382)	-
Transfer to Stage 2	(1,336)	1,687	(351)	-
Transfer to Stage 3	(178)	(720)	898	-
Net remeasurement of loss allowance	(1,216)	145	2,727	1,656
New financial assets originated or purchased	1,803	278	353	2,434
Derecognitions and maturities	(430)	(169)	(188)	(787)
Write-offs	-	(4)	(1,616)	(1,620)
Recoveries of amounts previously written off	-	-	249	249
Foreign exchange	-	-	10	10
Unwinding of interest	-	-	311	311
At 31 December 2019	3,645	953	5,700	10,298

Off-balance sheet loan commitments and financial guarantees

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	403	55	231	689
Transfer to Stage 1	230	(146)	(84)	-
Transfer to Stage 2	(74)	252	(178)	-
Transfer to Stage 3	(11)	(53)	64	-
Net remeasurement of loss allowance	(466)	269	103	(94)
New loan commitments and financial guarantees	376	166	128	670
Derecognitions and maturities	(111)	(60)	(39)	(210)
At 31 December 2020	347	483	225	1,055
At 1 January 2019	410	142	84	636
Transfer to Stage 1	152	(81)	(71)	-
Transfer to Stage 2	(20)	39	(19)	-
Transfer to Stage 3	(9)	(18)	27	-
Net remeasurement of loss allowance	(455)	(27)	131	(351)
New loan commitments and financial guarantees	447	20	119	586
Derecognitions and maturities	(122)	(20)	(40)	(182)
At 31 December 2019	403	55	231	689

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28. Investments in associates

		31.12.2020	31.12.2019
Auðkenni hf., an information security company, Borgartún 31, 105 Reykjavík	Iceland	23.8%	23.8%
JCC ehf., a cash centre service company, Sundaborg 15, 108 Reykjavík	Iceland	33.3%	33.3%
Reiknistofa bankanna hf., an IT service centre company, Katrínartún 2, 105 Reykjavík	Iceland	30.1%	30.8%

	2020	2019
Investments in associates at the beginning of the year	746	682
Share of gain of associates	44	64
Transfer to "Non-current assets and disposal groups held for sale"	(15)	-
Investments in associates	775	746

Summarised financial information in respect of the Group's associates is set out below:

	2020	2019
Revenue	6,388	6,259
Profit	296	281
Assets	5,651	5,445
Liabilities	(2,808)	(2,832)
Net assets	2,843	2,613
Group's share of net assets of associates	775	746

29. Property and equipment

At 31 December 2020	Land and buildings	Right-of-use assets: Buildings	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	4,096	4,634	4,068	12,798
Additions during the year	35	-	441	476
Disposals and write-offs during the year	(120)	(69)	(583)	(772)
Remeasurement	-	184	-	184
Transfer to "Non-current assets and disposal groups held for sale"	(953)	(20)	(807)	(1,780)
Historical cost	3,058	4,729	3,119	10,906
Balance at the beginning of the year	(1,447)	(420)	(1,763)	(3,630)
Depreciation during the year	(19)	(421)	(398)	(838)
Disposals and write-offs during the year	17	(67)	455	405
Transfer to "Non-current assets and disposal groups held for sale"	109	2	387	498
Accumulated depreciation	(1,340)	(906)	(1,319)	(3,565)
Carrying amount	1,718	3,823	1,800	7,341
Annual depreciation rates	0-2%	8-31%	8-33%	

Official real estate value of land and buildings	1,497
Insurance value of buildings	2,369
Insurance value of fixtures, equipment and vehicles	1,991

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29. Cont'd

At 31 December 2019	Land and buildings	Right-of-use assets: Land, buildings & vehicles	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	4,054	-	3,984	8,038
Impact of adopting IFRS 16	-	4,505	-	4,505
Additions during the year	56	3	271	330
Disposals and write-offs during the year	(14)	-	(187)	(201)
Remeasurement	-	126	-	126
Historical cost	4,096	4,634	4,068	12,798
Balance at the beginning of the year	(1,402)	-	(1,365)	(2,767)
Depreciation during the year	(47)	(420)	(574)	(1,041)
Disposals and write-offs during the year	2	-	176	178
Accumulated depreciation	(1,447)	(420)	(1,763)	(3,630)
Carrying amount	2,649	4,214	2,305	9,168
Annual depreciation rates	0-2%	3-33%	8-35%	

Official real estate value of land and buildings	2,240
Insurance value of buildings	3,545
Insurance value of fixtures, equipment and vehicles	2,020

30. Intangible assets

At 31 December 2020	Purchased software	Developed software	Goodwill	Total
Balance at the beginning of the year	1,782	3,383	318	5,483
Additions during the year and internal development	257	-	-	257
Write-offs during the year	(139)	-	-	(139)
Transfer to "Non-current assets and disposal groups held for sale"	(277)	-	(318)	(595)
Historical cost	1,623	3,383	-	5,006
Balance at the beginning of the year	(528)	(625)	-	(1,153)
Amortisation during the year	(346)	(267)	-	(613)
Write-offs during the year	110	-	-	110
Transfer to "Non-current assets and disposal groups held for sale"	128	-	-	128
Accumulated amortisation	(636)	(892)	-	(1,528)
Carrying amount	987	2,491	-	3,478
Amortisation rates	10-25%	10%	-	

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30. Cont'd

At 31 December 2019	Purchased software	Developed software	Goodwill	Total
Balance at the beginning of the year	1,639	3,644	248	5,531
Additions during the year and internal development	169	7	70	246
Write-offs during the year	(26)	(268)	-	(294)
Historical cost	1,782	3,383	318	5,483
Balance at the beginning of the year	(222)	(307)	-	(529)
Amortisation during the year	(313)	(318)	-	(631)
Write-offs during the year	7	-	-	7
Accumulated amortisation	(528)	(625)	-	(1,153)
Carrying amount	1,254	2,758	318	4,330
Amortisation rates	10-25%	10-25%	-	

31. Other assets

	31.12.2020	31.12.2019
Receivables	1,767	4,810
Unsettled securities transactions	1,550	279
Accruals	200	253
Prepaid expenses	181	468
Deferred tax assets	259	476
Other assets	168	322
Other assets	4,125	6,608

32. Non-current assets and disposal groups held for sale

	31.12.2020	31.12.2019
Repossessed collateral:		
Land and buildings	1,548	739
Industrial equipment and vehicles	7	44
Assets of disposal groups classified as held for sale	1,618	292
Non-current assets and disposal groups held for sale	3,173	1,075

At year-end 2020 the Group classified the assets and liabilities of BVS ehf. (63.5%) and Miðengi ehf. (100%) as assets and liabilities of disposal groups held for sale.

Assets and liabilities of disposal groups classified as held for sale:

	31.12.2020	31.12.2019
Shares	1,266	1
Receivables	224	90
Land and buildings	100	165
Other assets	28	36
Total assets	1,618	292
Other liabilities	27	-
Total liabilities	27	-

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33. Deposits from Central Bank and credit institutions

	31.12.2020	31.12.2019
Deposits from credit institutions	39,650	30,808
Repurchase agreements with Central Bank	108	117
Deposits from Central Bank and credit institutions	39,758	30,925

34. Deposits from customers

	31.12.2020	31.12.2019
Demand deposits and deposits with maturity up to 3 months	582,746	530,960
Term deposits with maturity of more than 3 months	96,709	87,353
Deposits from customers	679,455	618,313

Deposits from customers specified by owners	31.12.2020		31.12.2019	
	Amount	% of total	Amount	% of total
Central government and state-owned enterprises	8,145	1%	12,553	2%
Municipalities	7,561	1%	5,619	1%
Companies	326,799	48%	299,204	48%
Individuals	336,950	50%	300,937	49%
Deposits from customers	679,455	100%	618,313	100%

35. Pledged assets

	31.12.2020	31.12.2019
Financial assets pledged as collateral against liabilities	236,901	201,249
Financial assets pledged as collateral with the Central Bank	5,088	5,914
Financial assets pledged as collateral in foreign banks	167	402
Pledged assets against liabilities	242,156	207,565

The Group has pledged assets against the issuance of covered bonds under Icelandic law, which are pledged on a pool of consumer mortgage loans.

The Group has also pledged assets with the Central Bank to ensure the clearing of the Icelandic payment system as well as other contracts with the Central Bank.

The Group has also pledged cash in foreign banks and financial institutions, mainly as collateral for trades under ISDA agreements to hedge market risk.

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36. Debt issued and other borrowed funds

	Issued	Maturity		Interest	31.12.2020	31.12.2019
Covered bonds in ISK	2019-2020	2021	At maturity	Fixed rates	5,076	3,918
Covered bonds in ISK	2015-2020	2023	At maturity	Fixed rates	29,496	20,170
Covered bonds in ISK	2020	2027	Amortising	Fixed rates	5,386	-
Covered bonds in ISK - CPI-linked	2014-2015	2020	At maturity	Fixed rates	-	4,359
Covered bonds in ISK - CPI-linked	2015-2017	2022	At maturity	Fixed rates	19,228	18,512
Covered bonds in ISK - CPI-linked	2012-2018	2024	At maturity	Fixed rates	36,797	35,752
Covered bonds in ISK - CPI-linked	2015-2018	2026	At maturity	Fixed rates	28,571	27,661
Covered bonds in ISK - CPI-linked	2019-2020	2028	Amortising	Fixed rates	25,606	14,228
Covered bonds in ISK - CPI-linked	2017-2018	2030	At maturity	Fixed rates	26,285	25,463
Covered bonds					176,445	150,063
Senior unsecured bonds in EUR**	2016	2020	At maturity	Fixed rates	-	7,782
Senior unsecured bonds in SEK*	2019	2020	At maturity	Floating rates	-	4,557
Senior unsecured bonds in SEK	2018	2021	At maturity	Fixed rates	1,553	1,308
Senior unsecured bonds in SEK*	2018-2019	2021	At maturity	Floating rates	21,462	18,913
Senior unsecured bonds in EUR	2019	2021	At maturity	Floating rates	1,795	1,559
Senior unsecured bonds in SEK	2018	2022	At maturity	Floating rates	15,574	12,990
Senior unsecured bonds in EUR**	2019	2022	At maturity	Fixed rates	47,494	41,570
Senior unsecured bonds in NOK	2019	2022	At maturity	Floating rates	14,982	13,856
Senior unsecured bonds in EUR***	2018	2024	At maturity	Fixed rates	48,032	41,816
Senior unsecured bonds in NOK	2019	2024	At maturity	Fixed rates	6,187	5,709
Senior unsecured bonds in ISK	2019	2024	Monthly	Floating rates	2,664	3,553
Senior unsecured bonds in EUR**	2020	2023	At maturity	Fixed rates	46,944	-
Senior unsecured bonds in ISK	2020	2025	At maturity	Fixed rates	2,709	-
Bonds issued					209,396	153,613
Bills issued					1,433	2,705
Debt issued and other borrowed funds					387,274	306,381

*The Bank repurchased own bonds during the year amounting to ISK 6,084 million.

**These bond issuances are classified as being designated as at fair value through profit or loss. At 31 December 2020 the total carrying amount of the bonds amounted to ISK 94,438 million and included in the amount are fair value changes amounting to ISK 729 million. The carrying amount of the bonds at 31 December 2020 was ISK 16 million higher than the contractual amount due at maturity.

***The Group applies hedge accounting to this bond issuance and uses certain EUR denominated interest rate swaps as hedging instruments (see Note 25). The interest rate swaps are hedging the exposure of the Group's changes in the fair value of this fixed-rate EUR denominated bond arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 31 December 2020 the total carrying amount of the bond issuance amounted to ISK 48,032 million and included in the amount are fair value changes amounting to ISK 824 million.

The Bank has issued additional covered bonds for its own use, for example for the purpose of securities lending with regards to market making agreements. These covered bond amounts are not included in the total.

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37. Subordinated loans

	Issued	Maturity		Interest	31.12.2020	31.12.2019
Loans which qualify as Tier 2 capital:						
Subordinated loans in SEK	2017	2027	At maturity	Floating, STIBOR + 2.0%	11,646	9,714
Subordinated loans in SEK	2018	2028	At maturity	Floating, STIBOR + 2.5%	7,775	6,485
Subordinated loans in SEK	2019	2029	At maturity	Floating, STIBOR + 3.9%	7,773	6,475
Subordinated loans					27,194	22,674

38. Changes in liabilities arising from financing activities

			Non-cash changes			
	1.1.2020	Cash flows	Interest expense	Foreign exchange	Fair value changes	31.12.2020
Covered bonds in ISK	24,088	14,400	1,470	-	-	39,958
Covered bonds in ISK - CPI-linked	125,975	2,532	7,980	-	-	136,487
Senior unsecured bonds in ISK	3,553	1,728	92	-	-	5,373
Senior unsecured bonds FX	58,892	(7,093)	1,013	8,741	-	61,553
Senior unsecured bonds FX at fair value	49,352	38,069	608	6,468	(59)	94,438
Senior unsecured bonds used for hedging	41,816	(463)	566	6,061	52	48,032
Other borrowed funds	2,705	(1,330)	58	-	-	1,433
Subordinated loans	22,674	(738)	763	4,495	-	27,194
Total	329,055	47,105	12,550	25,765	(7)	414,468

			Non-cash changes			
	1.1.2019	Cash flows	Interest expense	Foreign exchange	Fair value changes	31.12.2019
Covered bonds in ISK	20,756	2,060	1,272	-	-	24,088
Covered bonds in ISK - CPI-linked	118,057	1,263	6,655	-	-	125,975
Senior unsecured bonds in ISK	-	3,528	25	-	-	3,553
Senior unsecured bonds FX	46,162	12,139	1,016	(425)	-	58,892
Senior unsecured bonds FX at fair value	68,154	(22,509)	734	1,667	1,306	49,352
Senior unsecured bonds used for hedging	40,714	(465)	497	786	284	41,816
Other borrowed funds	7,133	(4,809)	358	23	-	2,705
Subordinated loans	16,216	6,190	501	(233)	-	22,674
Total	317,192	(2,603)	11,058	1,818	1,590	329,055

39. Tax assets and tax liabilities

	31.12.2020		31.12.2019	
	Assets	Liabilities	Assets	Liabilities
Current tax	-	5,448	-	6,670
Deferred tax	259	2	476	1,183
Tax in the balance sheet	259	5,450	476	7,853

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39. Cont'd

	Assets	Liabilities
Deferred tax assets and tax liabilities 1.1.2019	215	678
Calculated income tax for 2019	256	3,223
Income tax payable in 2020	-	(2,535)
Income tax recognised in other comprehensive income	9	(183)
Prior year's income tax adjustment	(4)	-
Deferred tax assets and tax liabilities 31.12.2019	476	1,183
Calculated income tax for 2020	229	1,902
Income tax payable in 2021	-	(3,109)
- thereof income tax recognised in other comprehensive income	-	12
Changes in deferred tax assets and deferred tax liabilities due to equity	-	26
Transfer to "Non-current assets and disposal groups held for sale"	(446)	-
Deferred tax assets and tax liabilities 31.12.2020	259	2

2020	Net balance at 1 January	Transfer to non-current assets	Recognised in profit or (loss)	Recognised in equity	Balance at 31 December Net	Deferred tax assets	Deferred tax liabilities
Property and equipment	(1,097)	32	87	-	(978)	-	(978)
Intangible assets	(511)	-	21	-	(490)	-	(490)
Assets and liabilities in foreign currency	(276)	-	(144)	-	(420)	-	(420)
Deferred foreign exchange difference	(426)	(9)	1,540	-	1,105	1,105	-
Derivatives	(42)	22	(70)	-	(90)	-	(90)
Lease liabilities	851	-	(54)	-	797	797	-
Debt issued and other borrowed funds	268	4	6	(38)	240	240	-
Other items	30	-	63	-	93	93	-
Tax loss carry forwards	496	(496)	-	-	-	-	-
	(707)	(447)	1,449	(38)	257	2,235	(1,978)
Set-off of deferred tax assets together with liabilities of the same taxable entities						(1,976)	1,976
Tax assets (liabilities)	(707)	(447)	1,449	(38)	257	259	(2)

2019	Net balance at 1 January	Recognised in profit or (loss)	Recognised in equity	Balance at 31 December Net	Deferred tax assets	Deferred tax liabilities
Property and equipment	(249)	(848)	-	(1,097)	-	(1,097)
Intangible assets	(527)	16	-	(511)	-	(511)
Assets and liabilities in foreign currency	(264)	(12)	-	(276)	-	(276)
Deferred foreign exchange difference	(213)	(213)	-	(426)	-	(426)
Derivatives	194	(236)	-	(42)	-	(42)
Lease liabilities	-	851	-	851	851	-
Debt issued and other borrowed funds	329	(253)	192	268	268	-
Other items	(2)	32	-	30	30	-
Tax loss carry forwards	269	227	-	496	496	-
	(463)	(436)	192	(707)	1,645	(2,352)
Set-off of deferred tax assets together with liabilities of the same taxable entities					(1,169)	1,169
Tax assets (liabilities)	(463)	(436)	192	(707)	476	(1,183)

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40. Other liabilities

	31.12.2020	31.12.2019
Accruals	2,311	3,217
Liabilities to retailers for credit cards	-	14,765
Lease liabilities	3,962	4,256
Provision for effects of court rulings	288	75
Expected credit loss for off-balance sheet loan commitments and financial guarantees	1,055	689
Withholding tax	915	1,559
Unsettled securities transactions	1,379	515
Deferred income	-	229
Sundry liabilities	1,983	1,758
Non-current liabilities and disposal groups held for sale	27	-
Other liabilities	11,920	27,063

41. Custody assets

	31.12.2020	31.12.2019
Custody assets - not managed by the Group	2,863,328	2,496,313

42. Leases

The Group as a lessee

The Group's significant leases are leases for offices, branches, and storage. Most leases are CPI-linked real estate leases with duration of 5-10 years with extension options. Lease commitments are recognised on-balance sheet except for short-term leases and leases of low-value assets. During the year 2020 the total expense for leases of low-value assets and short-term leases amounted to ISK 23 million (2019: ISK 21 million). During the year 2020 the total cash outflow for leases amounted to ISK 500 million (2019: ISK 493 million).

Right-of-use assets are presented in the line item “Property and equipment” (see Note 29). Lease liabilities are presented in the line item “Other liabilities” (see Note 40). Interest expense from lease liabilities is presented in the line item "Interest expense" (see Note 8).

The Group as a lessor

Net investment in finance lease receivables

	31.12.2020	31.12.2019
Due within 1 year	14,030	17,559
Due in 1-5 years	31,152	30,960
Due in more than 5 years	3,132	3,538
Total gross investment in the lease	48,314	52,057
Due within 1 year	12,263	15,303
Due in 1-5 years	28,380	27,628
Due in more than 5 years	2,716	2,692
Total present value of lease payments*	43,359	45,623
Unearned interest income	4,955	6,434

*The Group presents finance lease receivables in the line item “Loans to customers”.

Expected credit loss allowance	990	202
Interest income from finance lease receivables during the year	2,439	3,165

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43. Related party

Íslandsbanki is wholly owned by the Icelandic Government. The shares are administered by the Icelandic State Financial Investments (ISFI). As a result, the Icelandic Government and the Icelandic State Financial Investments are defined as related parties. The Group has applied the partial exemption for government-related entities, as described in IAS 24, and does not disclose those transactions in the related party Note.

The Board of Directors and key management personnel of the Bank, ISFI and subsidiaries of the Bank, close family members of individuals referred to herein and legal entities controlled by them, are defined as related parties.

The Group's associates are also defined as related parties.

The Group's products and services are offered to the Icelandic Government and government-related entities in competition with other vendors and under generally accepted commercial terms. In a similar manner the Group entities purchase products and services from government-related entities under generally accepted commercial terms. Transactions with related parties were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third party counterparties.

Cash and balances with the Central Bank are disclosed under Note 23 and Deposits from the Central Bank are disclosed under Note 33.

All loans to employees are provided on general business terms of the Group and the balances do not reflect collaterals held by the Group.

At 31 December 2020	Assets	Liabilities	Net balance	Commitments, guarantees & overdrafts
Shareholders with control over the Group	-	-	-	3
Board of Directors, key management personnel and other related parties	440	393	47	45
Associated companies	31	342	(311)	228
Balances with related parties	471	735	(264)	276

2020	Interest income	Interest expense	Other income	Other expense
Board of Directors, key management personnel and other related parties	16	9	4	-
Associated companies	-	7	-	1,627
Transactions with related parties	16	16	4	1,627

At 31 December 2019	Assets	Liabilities	Net balance	Commitments, guarantees & overdrafts
Board of Directors, key management personnel and other related parties	324	392	(68)	51
Associated companies	16	830	(814)	213
Balances with related parties	340	1,222	(882)	264

2019	Interest income	Interest expense	Other income	Other expense
Board of Directors, key management personnel and other related parties	25	7	1	-
Associated companies	7	17	3	1,620
Transactions with related parties	32	24	4	1,620

At year-end 2020 there were no expected credit loss balances outstanding with related parties (2019: ISK 2 million). No share option programmes were operated during the year. For related party remuneration see Note 13.

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44. Contingencies

Contingent liabilities

Borgun hf. – Landsbanki case

Borgun hf., a former subsidiary of Íslandsbanki, is a payment acquirer and issuing processor. Landsbankinn hf. sold its 31.2% stake in Borgun hf. in late 2014. Landsbankinn claims that Borgun's management did not disclose all available information that might have affected the value of Borgun hf. during the sales process, namely the value of its stake in Visa Europe which was sold to Visa International shortly after the Borgun hf. sale. In order to reclaim the alleged loss, Landsbankinn filed a lawsuit against Borgun hf. and others on 12 January 2017, claiming the right to damages for having been deprived of the true value of the stake involved in the sale. Landsbankinn does not quantify the claim, but its estimate of the lost profit from having sold its shares in Borgun hf. is approximately ISK 1,930 million. Court appointed assessors presented their assessment in November 2019. A reassessment has been demanded and senior assessors have been appointed by the court. It is uncertain when a ruling is to be expected. In 2020, the Group closed an agreement on the sale of all its stake in Borgun hf. In that agreement Íslandsbanki undertook to reimburse 63.47% of losses incurred by Borgun hf. or the buyer as a result of an unfavourable outcome in the Landsbanki case. The Group has not recognised a provision as a result of this event.

45. Events after the reporting period

No events have arisen after the reporting period that require amendments or additional disclosures in the consolidated financial statements for the year ended 31 December 2020.

46. Risk management

Risk governance

The Group is exposed to various risk factors and managing these risks is an integral part of its operations. The Bank emphasises sound governance principles. The risk management and internal control framework of the Group is based on a three lines of defence model, as referred to in the European Banking Authority Guidelines on Internal Governance, and aims for informed decision-making and strong risk awareness. 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 Group’s internal rules.

The first line of defence consists of the Bank's business and support units; the second line of defence comprises the Bank's internal control units, Risk management and Compliance; and the third line of defence is Internal Audit which gives the Board an independent assessment of the quality of corporate governance, risk management and internal controls.

The Group's management body has a dual structure. The Board of Directors of the Bank has a supervising role in setting and monitoring the execution of set policies, the sound control of accounting and financial management and ensuring that group Internal audit, Compliance and Risk management are effective. The Chief Executive Officer (CEO), the Chief Risk Officer (CRO), other members of the senior management and the senior management committees are responsible for implementing risk management practises and internal monitoring in accordance with Board authorisation.

The ultimate responsibility for ensuring an adequate risk management and internal control framework at the Group lies with the Board of Directors. The Board defines and communicates the risk governance framework and the acceptable level of risk through risk management policies and the Risk Appetite Statement. To assist the Board in fulfilling its oversight responsibilities, the Board has appointed three board subcommittees.

The CEO is responsible for the day-to-day operations of the Bank, pursuant to set policies and resolutions of the Board. Moreover, it is the task of the CEO to ensure that the Group's operations are consistent with applicable legislation and the Group's Articles of Association which includes maintaining adequate and effective risk management and internal control functions. The CEO appoints the Chief Risk Officer, the Compliance Officer as well as other members of the Executive Board. The CEO also engages the members of the senior management committees.

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The CRO heads the Risk management function and is responsible for defining the daily tasks of the department and to assess the adequacy of its professional skills. In addition, the CRO is responsible for monitoring the risk management framework at the Group and for verifying that the Bank has the right resources and an appropriate organisation to manage its risks efficiently.

The CRO is selected and appointed by the CEO, subject to Board confirmation. The CRO reports directly to the Board and the Board Risk Committee on the overall risk profile of the Group and cannot be removed without the Board's prior approval.

The CRO is independent from the business units, is a member of the Executive Board and reports directly to the CEO. The CRO provides an independent view on the Group's exposure to risk. The CRO has the right but not the responsibility to veto certain risk-taking decisions of the senior management committees if an internal control unit considers the proposal inconsistent with the Bank's risk appetite, policies or procedures.

Risk management is mandated to identify, understand, measure and monitor the risks that the Group is exposed to. It provides independent information, analyses and expert judgement on risk exposures, and advice on proposals and risk decisions made by the management and business or support units as to whether they are consistent with the risk appetite and risk polices set by the Board.

Where necessary, Risk management makes recommendations to senior management and the Board to improve or clarify risk policies, procedures and limits.

Risk Management provides a holistic view on risk, and compliance to limits to internal and external stakeholders, and ensures an appropriate escalation in the event of limit breaches.

Business and support units are, however, responsible for maintaining their independent view on the risks inherent in their operations and reporting to senior management any foreseeable breaches from limits, policies or strategic direction.

Risk management provides the senior management and the Board with all relevant risk related information to enable it to define the Bank's risk appetite.

The General Counsel is appointed by and reports directly to the CEO. The General Counsel provides legal advice to the Bank's senior management, including the Board of Directors, and manages the Bank's legal department which provides comprehensive legal advice to the Bank's business segments and support units.

The Chief Audit Executive (CAE) is appointed by the Board, reports directly to Board and directs Group Internal Audit with a mandate from the Board. The CAE is responsible for internal audit matters within the Group, including internal audit tasks which have been outsourced.

The Compliance Officer heads the compliance function and is responsible for defining the daily tasks of the department and assessing the adequacy of its professional skills. The Compliance Officer is responsible for monitoring the compliance risk management framework for the Bank and maintaining oversight for compliance risk throughout the Bank.

The Bank's Compliance Officer is selected and engaged by the CEO, subject to Board confirmation. The Compliance Officer cannot be removed without the Board's prior approval. The Financial Supervisory Authority of the Central Bank and Chief Audit Executive shall be notified of the dismissal or departure of the Compliance Officer.

The Compliance Officer reports directly to the Board on the overall compliance risk profile of the Bank.

Each employee is responsible for understanding the risk related to their day-to-day work, for knowing and understanding the respective internal and external rules and procedures, for using the alert procedures in the event of possible fraudulent activities and for conducting business in accordance with the Bank's code of conduct.

The Bank's senior management committee structure is twofold. Firstly the two executive committees, the Executive Board and the All Risk Committee, that are responsible for the implementation of the Board approved business strategy, risk appetite and policies. Secondly the four business committees, the Asset and Liability Committee (ALCO), the Senior Credit Committee (SCC), the Investment Committee (IC) and the Operational and Security Committee (OSC), which are responsible for the approval of business or operational proposals subject to internal rules and guidelines issued by the executive committees and the Board.

The members of the senior management committees are appointed by the CEO, and their mandate and rules of procedure are documented in a charter issued by the CEO.

More information about the Group's risk management and risk assessment processes is available in the unaudited Pillar 3 2020 Report, which is available on the Bank's website: www.islandsbanki.is.

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47. Credit risk

Credit risk is defined as current or prospective risk to earnings and capital arising from an obligor's potential failure to meet the terms of any financial contract with the Group.

Credit concentration risk is the significantly increased risk that is driven by common underlying factors, e.g. industrial sector, economy, geographical location, type of financial instrument or due to connections or relations among counterparties. This includes exposures to parties under common control and significant exposures to groups of counterparties whose likelihood of default is driven by common underlying factors.

Credit risk arises principally from loans and advances to customers and other banks but also from balances with the Central Bank and off-balance sheet items such as financial guarantees, loan commitments and derivatives.

The Group has policies and procedures dedicated to accepting, measuring, and managing credit risk. The objective of the Group's credit risk management is to achieve an appropriate balance between risk and return and to minimise potential adverse effects of credit risk on the Group's financial performance.

A thorough analysis of the counterparty's financial standing, analysis of past and estimated future cash flows as well as the borrower's general ability to repay its obligations forms the basis for all credit decisions. The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, groups of borrowers, countries and industry segments. The Group measures and consolidates its credit risk for each counterparty or group of connected clients in accordance with internal and external criteria of connection between parties.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security in borrower's assets. The principal collateral types for loans are properties, vehicles, equipment, vessels and securities. When applicable, other credit risk mitigants are employed.

48. Maximum credit exposure

The Group's credit risk exposure comprises both on-balance sheet and off-balance sheet items. Maximum exposure to credit risk for on-balance sheet assets is the net carrying amount as reported in the statement of financial position. The maximum exposure for off-balance sheet items is the amount that the Group might have to pay out against financial guarantees and loan commitments, less provisions that have been made because of these items. The maximum credit exposure for a derivative contract is calculated by adding potential future credit exposure to the positive market value of the contract.

The industry breakdown shows the credit exposure by industry classification. The breakdown follows an internal industry classification which is based on the Icelandic ISAT2008 that derives from the European NACE Rev. 2 classification standard.

The Government guarantee schemes issued in response to the COVID-19 pandemic are presented in the line item “Loans to customers”. Of these, ISK 2,236 million are subject to 100% Government guarantee, ISK 1,034 million to 85% Government guarantee and ISK 400 million to 70% Government guarantee.

As a part of the agreement on the sale of Borgun hf. the Group took on certain guarantees with regards to chargeback risk that Borgun hf. is exposed to through its operations, which at year-end 2020 amount to about ISK 370 million. These guarantees are not included in the table below.

The Group's credit exposure, before taking account of any collateral held or other credit enhancements, is as follows:

At 31 December 2020	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	78,948	-	-	-	-	-	-	-	-	-	78,948
Loans to credit institutions	-	-	-	-	-	89,920	-	-	-	-	-	89,920
Bonds and debt instruments	-	107,502	22	-	1,257	18,192	116	7	191	929	-	128,216
Derivatives	-	165	66	-	-	8,436	239	669	-	65	273	9,913
Loans to customers:	437,377	-	124,260	42,352	8,673	1,539	78,561	23,440	10,911	157,502	122,102	1,006,717
Overdrafts	10,506	-	12,117	3,104	10	1,097	5,915	954	949	2,422	5,138	42,212
Credit cards	14,942	-	1,170	247	6	14	318	23	77	62	29	16,888
Mortgages	377,155	-	-	-	-	-	-	-	-	-	-	377,155
Capital leases	5,612	-	26,236	2,742	16	-	7,328	153	38	1,058	176	43,359
Government guarantee schemes	15	-	2,968	57	-	-	323	9	-	136	86	3,594
Other loans	29,147	-	81,769	36,202	8,641	428	64,677	22,301	9,847	153,824	116,673	523,509
Other financial assets	437	645	110	10	6	2,285	29	39	88	35	8	3,692
Off-balance sheet items:	33,695	-	29,294	13,373	316	7,376	26,056	1,531	5,348	21,209	14,190	152,388
Financial guarantees	489	-	5,349	6,786	-	90	2,077	30	6	8,090	272	23,189
Undrawn loan commitments	-	-	5,445	3,111	-	-	17,896	846	-	10,145	2,583	40,026
Undrawn overdrafts	9,722	-	13,826	2,679	286	7,051	4,901	446	4,026	2,664	11,145	56,746
Credit card commitments	23,484	-	4,674	797	30	235	1,182	209	1,316	310	190	32,427
Maximum credit exposure	471,509	187,260	153,752	55,735	10,252	127,748	105,001	25,686	16,538	179,740	136,573	1,469,794

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At 31 December 2019	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	146,638	-	-	-	-	-	-	-	-	-	146,638
Loans to credit institutions	-	-	-	-	-	54,376	-	-	-	-	-	54,376
Bonds and debt instruments	-	33,007	-	-	125	16,131	1,296	52	1,027	1,232	-	52,870
Derivatives	-	-	706	-	1,836	5,788	189	530	-	208	228	9,485
Loans to customers:	349,181	-	126,488	44,420	7,887	2,315	82,288	23,590	12,312	145,559	105,592	899,632
Overdrafts	12,333	-	14,506	3,425	110	2,289	4,927	654	1,204	3,220	6,270	48,938
Credit cards	16,466	-	1,579	271	5	24	437	40	106	63	35	19,026
Mortgages	281,450	-	5	-	-	-	-	-	-	44	-	281,499
Capital leases	5,774	-	28,422	2,700	15	-	7,322	139	39	1,005	207	45,623
Other loans	33,158	-	81,976	38,024	7,757	2	69,602	22,757	10,963	141,227	99,080	504,546
Other financial assets	532	-	199	7	6	4,803	117	41	10	36	6	5,757
Off-balance sheet items:	33,964	-	24,605	16,035	2,974	6,579	18,865	548	3,461	19,036	9,738	135,805
Financial guarantees	1,477	-	6,035	4,914	-	1,172	2,907	95	5	2,004	252	18,861
Undrawn loan commitments	-	-	1,871	8,297	2,442	-	9,726	-	-	11,303	1,804	35,443
Undrawn overdrafts	9,842	-	12,476	2,063	503	5,291	5,135	314	2,733	5,456	7,525	51,338
Credit card commitments	22,645	-	4,223	761	29	116	1,097	139	723	273	157	30,163
Maximum credit exposure	383,677	179,645	151,998	60,462	12,828	89,992	102,755	24,761	16,810	166,071	115,564	1,304,563

49. Credit exposure covered by collateral

Collateral and other credit mitigants vary between types of obligors and credit facilities. Loans to credit institutions are usually unsecured. For loans to individuals the principal collateral taken is residential property against mortgages. In the case of corporate entities the Group takes a charge over assets such as real estate, vessels, cash and securities as well as other collateral including accounts receivables, inventory, vehicles and equipment. Loans to government entities and to municipalities are more often than not unsecured. Derivative exposures are generally made under ISDA master agreements with Credit Support Annex or corresponding terms with pledged collateral in the form of cash and government bonds.

In some cases the Group uses guarantees as a credit enhancement but since guarantees effectively transfer credit risk from one counterparty to another they do not represent a reduction in maximum exposure to credit risk. Exception from this are Government guarantees issued in response to the COVID-19 pandemic which are shown under other collateral. Covenants in loan agreements are also an important credit enhancement but do not reduce maximum credit exposure.

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Valuation of collateral is based on market price, official valuation for tax purposes or expert opinion of the Group's employees, depending on availability. In the case of fishing vessels the associated fishing quota is included in the valuation. Collateral is allocated according to the gross carrying amount of loans and nominal off-balance sheet items, and is measured without including the effect of overcollateralisation. This means that if some loans have collateral values in excess of their gross carrying amount, then the excess is removed in order to reflect the Group's actual maximum exposure to credit risk. The total value of pledged assets can thus be higher than the cover indicates. The maximum credit risk exposure is measured on net carrying value basis, and therefore collateral allocation can in some instances be higher. For capital leases the Group remains the owner of the leased object. In total ISK 38,872 million of the collateral are leased objects.

The following tables show the maximum exposure to credit risk by class of financial asset and collateral held against those exposures. An overview of collateral held by the Group against credit exposure is shown below for exposures in Stages 1 and 2 (non credit-impaired) and exposures in Stage 3 (credit-impaired):

At 31 December 2020 **Collateral held against non credit-impaired exposures**	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral	Total credit exposure not covered by collateral	Associated ECL
Derivatives	9,913	-	-	5,318	-	-	5,318	4,595	-
Loans and commitments to customers:	1,136,660	706,096	95,947	11,869	49,504	102,673	966,089	170,571	10,957
Individuals	464,333	382,505	7	376	14,327	151	397,366	66,967	1,939
Commerce and services	149,751	61,610	157	659	25,444	32,211	120,081	29,670	4,029
Construction	54,812	41,329	11	1,297	2,108	2,249	46,994	7,818	570
Energy	8,989	6,545	-	1	14	14	6,574	2,415	25
Financial services	8,915	1,083	-	26	-	3,543	4,652	4,263	2
Industrial and transportation	102,499	39,750	12	178	7,088	29,500	76,528	25,971	1,127
Investment companies	21,626	6,903	-	1,891	79	11,125	19,998	1,628	709
Public sector and non-profit organisations	16,258	1,007	-	5	28	-	1,040	15,218	20
Real estate	173,328	149,991	-	7,424	343	1,157	158,915	14,413	2,280
Seafood	136,149	15,373	95,760	12	73	22,723	133,941	2,208	256
Total	1,146,573	706,096	95,947	17,187	49,504	102,673	971,407	175,166	10,957
Collateral held against credit-impaired exposures									
Loans and commitments to customers:	22,445	14,644	1,556	2,704	725	917	20,546	1,899	7,612
Individuals	6,739	5,973	21	3	144	4	6,145	594	935
Commerce and services	3,803	1,706	691	3	232	780	3,412	391	2,573
Construction	913	630	-	-	87	50	767	146	151
Industrial and transportation	2,118	431	810	51	246	71	1,609	509	1,922
Investment companies	3,345	714	-	2,611	6	-	3,331	14	284
Public sector and non-profit organisations	1	1	-	-	-	-	1	-	-
Real estate	5,383	5,082	5	36	7	12	5,142	241	1,565
Seafood	143	107	29	-	3	-	139	4	182
Total	22,445	14,644	1,556	2,704	725	917	20,546	1,899	7,612

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At 31 December 2019 **Collateral held against non credit-impaired exposures**	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral	Total credit exposure not covered by collateral	Associated ECL
Derivatives	9,485	-	-	1,757	-	-	1,757	7,728	-
Loans and commitments to customers:	1,012,821	622,021	87,217	7,001	49,865	80,043	846,147	166,674	5,056
Individuals	374,718	292,701	7	417	13,317	116	306,558	68,160	1,579
Commerce and services	146,149	63,151	777	961	27,124	25,891	117,904	28,245	1,030
Construction	55,236	40,432	4	653	2,130	3,968	47,187	8,049	495
Energy	10,861	5,655	-	366	8	5	6,034	4,827	34
Financial services	8,894	-	-	123	-	3,621	3,744	5,150	7
Industrial and transportation	99,188	49,944	12	107	6,757	18,566	75,386	23,802	534
Investment companies	23,982	7,748	-	3,281	71	11,930	23,030	952	478
Public sector and non-profit organisations	15,758	958	-	7	29	-	994	14,764	29
Real estate	162,795	148,919	5	1,072	301	1,125	151,422	11,373	702
Seafood	115,240	12,513	86,412	14	128	14,821	113,888	1,352	168
Total	1,022,306	622,021	87,217	8,758	49,865	80,043	847,904	174,402	5,056
Collateral held against credit-impaired exposures									
Loans and commitments to customers:	22,616	17,100	1,481	333	846	830	20,590	2,026	5,931
Individuals	8,427	7,191	17	12	166	2	7,388	1,039	1,245
Commerce and services	4,944	2,980	102	22	561	805	4,470	474	1,864
Construction	5,219	4,919	-	197	19	7	5,142	77	261
Industrial and transportation	1,965	253	1,331	102	72	16	1,774	191	1,559
Investment companies	156	149	-	-	-	-	149	7	111
Public sector and non-profit organisations	15	14	-	-	-	-	14	1	1
Real estate	1,800	1,567	-	-	9	-	1,576	224	595
Seafood	90	27	31	-	19	-	77	13	295
Total	22,616	17,100	1,481	333	846	830	20,590	2,026	5,931

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50. Credit quality of financial assets

The following table provides the gross carrying amount of loans and credit risk exposure on loan commitments and financial guarantees. Amounts are broken down by risk class and the method by which their respective credit loss allowances (ECL) are calculated, i.e. Stage 1, 2 and 3.

The Group uses internal rating models to assess the default probability of corporate and retail customers. The models assign each customer to one of ten risk classes. One risk class is for customers in default (risk class 10), and nine risk classes are for performing customers (risk classes 1-9). Risk classes are assigned on customer level and not facility level.

The rating of corporate customers is based on a company's most recent financial statement, together with a qualitative assessment of its management, market position and industry sector.

For retail customers the Group uses two different statistical rating models. One model is for individuals and another is for small companies with a total exposure to the Group of less than ISK 150 million. These models are behavioural scoring models and use information about a customer's payment history, amount of debt and deposits, and demographic variables to assess the probability that a customer will default on any of his obligations within 12 months of the rating assessment.

Risk classes 1-4 represent low risk, risk classes 5-6 moderate risk, risk classes 7-8 increased risk, risk class 9 high risk, and risk class 10 represents customers that are in default. Unrated are loans that are yet to be rated.

Further information on the risk classes, including the mapping from risk classes to the probability of default, can be found in Section 4.2.2 of the unaudited Pillar 3 2020 Report.

The same customer can have loans and off-balance sheet commitments in Stages 1 and 2 simultaneously. However, if a customer has an exposure in Stage 3 then all other loans and commitments are classified as Stage 3 as well.

Due to the COVID-19 pandemic the Group transferred a relatively large proportion of assets from Stage 1 to Stage 2 in the first half of 2020. In addition to the move from 12-month to lifetime expected credit loss, an additional overlay factor was applied to customers in the tourism industry (see Note 3).

At 31 December 2020

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	232,806	1,209	-	234,015
Risk class 5-6	346,781	62,788	-	409,569
Risk class 7-8	217,368	80,867	-	298,235
Risk class 9	38,290	14,684	-	52,974
Risk class 10	-	-	29,247	29,247
Unrated	190	1	-	191
	835,435	159,549	29,247	1,024,231
Expected credit loss	(3,645)	(6,482)	(7,387)	(17,514)
Net carrying amount	831,790	153,067	21,860	1,006,717

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	64,781	1,341	-	66,122
Risk class 5-6	51,169	6,461	-	57,630
Risk class 7-8	10,852	16,227	-	27,079
Risk class 9	1,142	553	-	1,695
Risk class 10	-	-	809	809
Unrated	99	8	-	107
	128,043	24,590	809	153,442
Expected credit loss	(347)	(483)	(225)	(1,055)
Total	127,696	24,107	584	152,387

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At 31 December 2020	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	94,574	182,706	153,088	35,928	7,646	4	(2,874)	471,072
Commerce and services	25,813	62,494	58,182	7,121	6,402	144	(6,602)	153,554
Construction	4,809	22,332	26,078	2,130	1,064	33	(721)	55,725
Energy	5,006	3,338	670	-	-	-	(25)	8,989
Financial services	5,816	2,650	443	-	-	8	(2)	8,915
Industrial and transportation	15,557	56,578	28,547	2,895	4,039	50	(3,049)	104,617
Investment companies	868	5,171	14,695	1,599	3,628	2	(993)	24,970
Public sector and non-profit organisations	14,525	1,400	324	1	1	28	(20)	16,259
Real estate	46,297	82,945	42,299	4,057	6,950	8	(3,845)	178,711
Seafood	86,872	47,585	988	938	326	21	(438)	136,292
Total	300,137	467,199	325,314	54,669	30,056	298	(18,569)	1,159,104

At 31 December 2019

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	226,347	289	-	226,636
Risk class 5-6	388,936	1,385	-	390,321
Risk class 7-8	204,979	14,487	-	219,466
Risk class 9	33,880	7,544	-	41,424
Risk class 10	-	-	27,160	27,160
Unrated	4,676	93	154	4,923
	858,818	23,798	27,314	909,930
Expected credit loss	(3,645)	(953)	(5,700)	(10,298)
Net carrying amount	855,173	22,845	21,614	899,632

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	58,327	25	-	58,352
Risk class 5-6	58,271	253	-	58,524
Risk class 7-8	15,334	1,757	-	17,091
Risk class 9	1,095	186	-	1,281
Risk class 10	-	-	1,233	1,233
Unrated	8	5	-	13
	133,035	2,226	1,233	136,494
Expected credit loss	(403)	(55)	(231)	(689)
Total	132,632	2,171	1,002	135,805

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At 31 December 2019	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	76,119	151,224	115,042	29,537	9,517	4,530	(2,824)	383,145
Commerce and services	29,718	81,536	31,572	3,968	6,810	383	(2,894)	151,093
Construction	3,354	33,345	17,924	1,120	5,468	-	(756)	60,455
Energy	5,045	3,846	2,004	-	-	-	(34)	10,861
Financial services	8,848	30	17	-	-	6	(7)	8,894
Industrial and transportation	26,474	59,108	11,775	2,363	3,526	-	(2,093)	101,153
Investment companies	2,803	9,198	11,090	1,367	268	1	(589)	24,138
Public sector and non-profit organisations	12,761	2,733	268	11	15	15	(30)	15,773
Real estate	52,934	64,623	42,304	3,631	2,400	-	(1,297)	164,595
Seafood	66,932	43,202	4,561	708	389	1	(463)	115,330
Total	284,988	448,845	236,557	42,705	28,393	4,936	(10,987)	1,035,437

51. Loans to customers in the tourism industry likely to be vulnerable to COVID-19 pandemic

Companies susceptible to the impact of COVID-19 were classified into four groups based on an assessment of how much an increase in credit risk these companies face in the short, medium and long term. In addition, to account for the material uncertainty in the operating environment of companies in the tourism industry, not reflected in their current risk class, they are further classified into four groups based on an assessment of how vulnerable they are to various assumptions on when tourists can be expected to start visiting Iceland again. The base case assumes around 700.000 tourists in Iceland in 2021.

Impact group 1: viable even though significantly fewer tourists arrive in the year 2021
Impact group 2: viable with forbearance even though significantly fewer tourists arrive in the year 2021
Impact group 3: viable if the number of tourists in the year 2021 is similar to the base case
Impact group 4: viable if the year 2021 turns out to be better than the base case

Where the increase was found to be significant (groups 2-4), the exposure was transferred to Stage 2. In addition, an overlay factor was applied to the expected credit loss, comparable to an increase in up to three risk classes, and a higher haircut was applied to value of collateral for the higher impact groups in the more severe scenarios.

At 31 December 2020

Loans to customers in the tourism industry:	Stage 1	Stage 2	Stage 3	Total
Group 1	1,903	308	-	2,211
Group 2	-	30,503	406	30,909
Group 3	-	58,610	2,579	61,189
Group 4	-	3,317	3,612	6,929
	1,903	92,738	6,597	101,238
Expected credit loss	(24)	(4,483)	(2,529)	(7,036)
Net carrying amount	1,879	88,255	4,068	94,202

Off-balance sheet loan commitments and financial guarantees to customers in the tourism industry:

	Stage 1	Stage 2	Stage 3	Total
Group 1	50	2	-	52
Group 2	-	13,416	51	13,467
Group 3	-	5,118	163	5,281
Group 4	-	429	17	446
	50	18,965	231	19,246
Expected credit loss	(3)	(363)	(101)	(467)
Total	47	18,602	130	18,779

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52. Forbearance

When restructuring or modification measures are believed to be more appropriate than collection procedures, the Group offers several debt relief measures and restructuring frameworks for customers in financial difficulties. These forbearance measures include temporary payment holidays, extension of loan terms, capitalisation of arrears and waiving of covenants.

The relationship between forbearance and stages is discussed in Note 67.4.

Once an asset has been classified as forborne, it will remain forborne for a minimum 24-month probation period. In order for a loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:
- All of the customer's facilities have to be considered performing; and
- The customer does not have any contract that is more than 30 days past due; and
- The probation period of two years has passed from the date of the forbearance event; and
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period

Because of the COVID-19 pandemic, the Group entered into an agreement with other financial institutions and lenders in Iceland to provide a moratorium for customers, uniformly executed across institutions. In the interim financial statements for the third quarter of 2020 the Group showed the extent of the payment moratoria granted by the Group under these initiatives. The agreement expired on 30 September 2020 and all moratoria under it has expired. Further extensions of moratoria has been granted on a case-by-case basis and is now classified as forbearance.

The tourism industry is an important economic sector in Iceland but due to the nature of tourism, its effects are not limited to hotels, car rentals and tour guides. The Group therefore monitors the tourism industry internally as a quasi-sector instead of a new separate sector. Real estate companies that do not operate directly in the tourism sector but rely in part on rental income from such activities explain around half of the forbearance amount for companies not in tourism.

The following table provides a summary of the Group's forborne assets. The loans that previously were in payment moratorium and are now forborne are shown separately.

At 31 December 2020	Stage 1	Stage 2	Stage 3	Total
Individuals	932	5,249	2,068	8,249
- thereof previously in COVID-19 moratoria	83	3,031	55	3,169
Companies	209	104,523	13,608	118,340
- In the tourism quasi-sector	-	62,295	5,747	68,042
- thereof previously in COVID-19 moratoria	-	54,945	321	55,266
- Other than the tourism quasi-sector	209	42,228	7,861	50,298
- thereof previously in COVID-19 moratoria	40	24,038	35	24,113
Gross carrying amount	1,141	109,772	15,676	126,589

	Stage 1	Stage 2	Stage 3	Total
Individuals	(10)	(127)	(176)	(313)
- thereof previously in COVID-19 moratoria	-	(62)	(1)	(63)
Companies	(1)	(4,114)	(4,147)	(8,262)
- In the tourism quasi-sector	-	(2,787)	(1,888)	(4,675)
- thereof previously in COVID-19 moratoria	-	(2,508)	(136)	(2,644)
- Other than the tourism quasi-sector	(1)	(1,327)	(2,259)	(3,587)
- thereof previously in COVID-19 moratoria	-	(462)	(1)	(463)
Expected credit loss	(11)	(4,241)	(4,323)	(8,575)

At 31 December 2019	Stage 1	Stage 2	Stage 3	Total
Individuals	1,615	1,102	1,372	4,089
Companies	13,212	8,469	8,289	29,970
Gross carrying amount	14,827	9,571	9,661	34,059

	Stage 1	Stage 2	Stage 3	Total
Individuals	(12)	(41)	(182)	(235)
Companies	(77)	(249)	(2,167)	(2,493)
Expected credit loss	(89)	(290)	(2,349)	(2,728)

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53. Assets obtained by taking possession of collateral

Details of non-financial assets obtained by the Group during the year by taking possession of collateral held as security against loans.

	31.12.2020	31.12.2019
Property and land	1,754	378
Industrial equipment and vehicles	86	81
Total	1,840	459

The Group pursues realisation of the collateral in an orderly manner. The Group does not generally use the non-cash collateral for its own operations.

54. Write-offs

When the Group has no reasonable expectations of recovering a credit exposure or when it is uneconomical to pursue legal collection, the financial asset is written off. A write-off does not change the debt obligation which is therefore still subject to enforcement activity. Any recoveries of amounts previously written off are credited to the income statement.

Gross carrying amount written off and still subject to enforcement activity	2020	2019
Individuals	393	578
Companies	1,091	1,253
Total	1,484	1,831

55. Large exposures disclosure

When the Group's total exposure to a group of connected clients is 10% or higher of the Group's capital base it is considered a large exposure. Both on-balance sheet and off-balance sheet items from all types of financial instruments are included in the exposure as defined by regulation no. 233/2017. The Group has internal criteria that define connections between clients. These criteria reflect the Group's interpretation of Article (1)(a) of the Act on Financial Undertakings no. 161/2002, where groups of connected clients are defined.

The exposure is evaluated both before and after credit risk mitigating effects. After mitigating effects, the Group currently has one large exposure. No large exposure is therefore above the maximum 25% single large exposure limit set by the law.

The following tables show the Group's large exposures as a percentage of the Group's capital base, before and after eligible credit risk mitigating effects.

At 31 December 2020

Groups of connected clients:	Before	After
Group 1	65%	-
Group 2	13%	10%

At 31 December 2019

Groups of connected clients:	Before	After
Group 1	75%	-

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56. Liquidity risk

The Group defines liquidity risk as the risk of not being able to fund its financial obligations or planned growth, or only being able to do so substantially above the prevailing market cost of funds.

The Group's main source of funding is customer deposits. Treasury is responsible for the Bank's funding and liquidity management in line with internal and regulatory limits and policies. Treasury manages the Bank's intraday liquidity. Risk Management, as the second line of defence, is responsible for independent reporting on the liquidity position to internal and external stakeholders and providing a holistic view on liquidity risk on a consolidated basis.

57. Liquidity coverage and Net stable funding ratio

Key measures for the assessment of liquidity risk are the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). The Central Bank of Iceland, which is the main supervisory authority regarding liquidity risk, has incorporated the LCR and the NSFR based on the CRD IV standards into the rules on liquidity ratio and the rules on funding ratio in foreign currencies. In addition, the Group complies with the Financial Supervisory Authority of the Central Bank's guidelines no. 2/2010 on best practices in liquidity management and liquidity coverage ratio rules no. 266/2017.

The following tables show the NSFR and the LCR for the Group at year-end 2020 and 2019.

Net stable funding ratio	31.12.2020	31.12.2019
For all currencies	123%	119%
Foreign currencies	179%	156%

Liquidity coverage ratio	31.12.2020	31.12.2019
For all currencies	196%	155%
Domestic currency	95%	110%
Foreign currencies	463%	325%

At 31 December 2020	For all currencies		Domestic currency		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	182,104	182,104	138,078	138,078	44,027	44,027
Liquid assets level 2	14,648	2,941	14,470	2,941	178	-
Total liquid assets	196,752	185,045	152,548	141,019	44,205	44,027
Deposits	542,123	147,611	472,073	120,974	70,049	26,636
Debt issued	2,271	2,271	47	47	2,225	2,225
Other outflows	99,949	44,756	68,500	35,605	31,449	9,151
Total outflows	644,343	194,638	540,620	156,626	103,723	38,012
Short-term deposits with other banks**	88,495	88,328	2,077	2,077	86,419	86,252
Other inflows	29,842	11,981	21,342	6,221	8,500	5,760
Restrictions on inflows	-	-	-	-	(17,126)	(63,503)
Total inflows	118,337	100,309	23,419	8,298	77,793	28,509
Liquidity coverage ratio		196%		95%		463%

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At 31 December 2019	For all currencies		Domestic currency		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	157,080	157,080	125,222	125,222	31,858	31,858
Liquid assets level 2	11,942	6,271	8,216	5,751	3,727	520
Total liquid assets	169,022	163,351	133,438	130,973	35,585	32,378
Deposits	482,322	139,354	404,233	105,393	78,089	33,961
Debt issued	1,361	1,361	711	711	650	650
Other outflows	81,493	30,997	63,481	25,749	18,012	5,248
Total outflows	565,176	171,712	468,425	131,853	96,751	39,859
Short-term deposits with other banks**	54,203	52,335	2,860	2,074	51,343	50,261
Other inflows	33,984	14,213	27,697	10,655	6,287	3,558
Restrictions on inflows	-	-	-	-	-	(23,925)
Total inflows	88,187	66,548	30,557	12,729	57,630	29,894
Liquidity coverage ratio		155%		110%		325%

*Level 1 liquid assets include cash and balances with the Central Bank, domestic bonds eligible as collateral against borrowing at the Central Bank and foreign government bonds in accordance with rules no. 266/2017 on liquidity ratio.

**Short-tem deposits with other banks with maturity less than 30 days.

Deposits by liquidity coverage ratio category

The Group's deposits are categorised by counterparty according to the Liquidity Coverage Ratio (LCR) standard. The groups are listed in order of estimated stability and the respective LCR outflow weight. Deposits are also classified as stable if the customer has an established business relationship with the Bank and is covered by an effective insurance scheme.

Increase in compensation according to the insurance guarantee scheme in Iceland and the Bank's update of its internal definition of established business relationships caused the amount of stable deposits to increase compared to year-end 2019.

At 31 December 2020	Deposits maturing within 30 days					
	Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	120,510	14%	247,625	5%	75,971	444,106
Operational relationships	3,155	25%	-	5%	-	3,155
Corporations	77,705	40%	1,959	20%	24,965	104,629
Sovereigns, Central Bank and public sector entities	6,340	40%	1,174	20%	934	8,448
Pension funds	39,105	100%	-	-	23,754	62,859
Domestic financial entities	38,284	100%	-	-	41,647	79,931
Foreign financial entities	6,266	100%	-	-	9,819	16,085
Total	291,365		250,758		177,090	719,213

At 31 December 2019	Deposits maturing within 30 days					
	Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	228,447	12%	83,773	5%	78,870	391,090
Operational relationships	2,446	25%	-	5%	-	2,446
Corporations	73,739	40%	337	20%	24,589	98,665
Sovereigns, Central Bank and public sector entities	6,813	40%	253	20%	620	7,686
Pension funds	35,405	100%	-	-	24,869	60,274
Domestic financial entities	28,494	100%	-	-	46,371	74,865
Foreign financial entities	8,038	100%	-	-	6,174	14,212
Total	383,382		84,363		181,493	649,238

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58. Maturity analysis of assets and liabilities

The following tables show the maturity profile of the Group's financial assets and the undiscounted cash flows of its financial liabilities.

Maturity classification of assets is based on contractual maturity. For bonds and debt instruments in the banking book the maturity classification is based on contractual maturity while for bonds and debt instruments held for trading the maturity classification is based on the estimated liquidation time of the asset.

The tables show undiscounted contractual payments of principal and interest for the Group's financial liabilities. Thus, the total figures for each liability class are higher than the respective balance sheet amount. Cash flows for payments of unknown nature, such as for floating rate, CPI-linked or foreign currency denominated instruments, are based on internal yield curves and forecasts.

For dated financial liabilities the amounts are grouped into maturity buckets according to contractual maturities of principal and estimated contractual payments of interest. For demand deposits or other non-dated liabilities, the figures are grouped according to the first possible required payment date.

The contractual cash flow of the Group's derivative liabilities, i.e. derivatives that have a negative and a positive carrying amount at the reporting date. For derivatives settled on a gross basis, the cash flow for both legs of the derivative is shown, since netting cannot be applied upon settlement.

At 31 December 2020	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central Bank	78,948	29,600	48,060	-	-	1,288	-	78,948
Loans to credit institutions	89,920	46,102	43,818	-	-	-	-	89,920
Bonds and debt instruments	128,216	-	38,169	34,776	48,047	7,224	-	128,216
Loans to customers	1,006,717	2,562	81,090	96,084	334,520	492,461	-	1,006,717
Shares and equity instruments	14,851	-	-	-	-	-	14,851	14,851
Other financial assets	3,692	2,483	560	643	6	-	-	3,692
Total financial assets	1,322,344	80,747	211,697	131,503	382,573	500,973	14,851	1,322,344
Deposits from CB and credit institutions	39,758	6,073	20,044	10,278	3,368	-	-	39,763
Deposits from customers	679,455	539,932	65,532	56,764	23,409	27,016	-	712,653
Debt issued and other borrowed funds	387,274	-	12,677	31,569	327,003	93,434	-	464,683
Subordinated loans	27,194	-	176	477	3,096	29,903	-	33,652
Other financial liabilities:	9,721	3,570	1,453	1,227	1,783	2,123	-	10,156
Lease liabilities	3,962	-	123	369	1,783	2,123	-	4,398
Other liabilities	5,759	3,571	1,330	858	-	-	-	5,759
Total financial liabilities	1,143,402	549,575	99,882	100,315	358,659	152,476	-	1,260,907

	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	41,288	46,627	39,643	-	-	127,558
Outflow	-	(38,823)	(45,090)	(36,516)	-	-	(120,429)
Total	-	2,465	1,537	3,127	-	-	7,129
Net settled derivatives	-	90	-	-	-	-	90
Total derivative financial assets	-	2,555	1,537	3,127	-	-	7,219
Gross settled derivatives							
Inflow	-	29,311	18,714	29,943	-	-	77,968
Outflow	-	(30,236)	(20,113)	(33,957)	-	-	(84,306)
Total	-	(925)	(1,399)	(4,014)	-	-	(6,338)
Net settled derivatives	-	(1,752)	-	-	-	-	(1,752)
Total derivative financial liabilities	-	(2,677)	(1,399)	(4,014)	-	-	(8,090)
Total net financial assets and financial liabilities	(468,828)	117,047	34,124	31,055	348,497	14,851	76,746

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At 31 December 2019	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central Bank	146,638	28,978	115,981	-	-	1,679	-	146,638
Loans to credit institutions	54,376	20,719	33,656	-	-	-	-	54,375
Bonds and debt instruments	52,870	7,768	23,998	10,120	10,983	-	-	52,869
Loans to customers	899,632	2,972	88,446	87,462	303,668	417,083	-	899,631
Shares and equity instruments	18,426	-	-	-	-	-	18,426	18,426
Other financial assets	5,757	1,889	525	118	17	-	3,259	5,808
Total financial assets	1,177,699	62,326	262,606	97,700	314,668	418,762	21,685	1,177,747
Deposits from CB and credit institutions	30,925	1,992	16,363	8,468	4,580	-	-	31,403
Deposits from customers	618,313	453,959	78,232	54,994	16,612	62,222	-	666,019
Debt issued and other borrowed funds	306,381	-	6,991	24,861	267,776	90,610	-	390,238
Subordinated loans	22,674	-	158	463	2,865	26,482	-	29,968
Other financial liabilities:	24,772	17,581	2,124	1,276	1,759	2,448	-	25,188
Lease liabilities	4,256	-	116	349	1,759	2,448	-	4,672
Other liabilities	20,516	17,581	2,008	927	-	-	-	20,516
Total financial liabilities	1,003,065	473,532	103,868	90,062	293,592	181,762	-	1,142,816

	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	92,680	28,583	74,731	-	-	195,994
Outflow	-	(82,832)	(27,964)	(73,544)	-	-	(184,340)
Total	-	9,848	619	1,187	-	-	11,654
Net settled derivatives	-	273	-	-	-	-	273
Total derivative financial assets	-	10,121	619	1,187	-	-	11,927
Gross settled derivatives							
Inflow	-	57,542	36,133	43,218	-	-	136,893
Outflow	-	(59,615)	(37,222)	(44,915)	-	-	(141,752)
Total	-	(2,073)	(1,089)	(1,697)	-	-	(4,859)
Net settled derivatives	-	(323)	-	-	-	-	(323)
Total derivative financial liabilities	-	(2,396)	(1,089)	(1,697)	-	-	(5,182)
Total net financial assets and financial liabilities	(411,206)	171,255	9,346	23,960	237,000	21,685	52,040

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Off-balance sheet liabilities

The following tables show the amount of contractual obligations of off-balance sheet liabilities that the Group has taken towards customers, either by committing to lend out money in the future or as third party guarantees. The amounts shown reflect the maximum amount, not taking into account the Group's ability to reduce overdraft or credit card limits before the current undrawn amount is fully utilised by the customer. These obligations all fall into the first time bucket since contractually, on a case-by-case basis, the Group could be required to fulfil these obligations instantaneously.

At 31 December 2020	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	23,189	-	-	-	-	-	23,189
Undrawn loan commitments	40,026	-	-	-	-	-	40,026
Undrawn overdrafts	56,746	-	-	-	-	-	56,746
Credit card commitments	32,427	-	-	-	-	-	32,427
Total off-balance sheet liabilities	152,388	-	-	-	-	-	152,388
At 31 December 2019							
Financial guarantees	18,861	-	-	-	-	-	18,861
Undrawn loan commitments	35,443	-	-	-	-	-	35,443
Undrawn overdrafts	51,338	-	-	-	-	-	51,338
Credit card commitments	30,163	-	-	-	-	-	30,163
Total off-balance sheet liabilities	135,805	-	-	-	-	-	135,805

59. Market risk

The Group defines market risk as the current or prospective risk to earnings and capital arising from adverse movements in the level or volatility of prices of market instruments, such as those that arise from changes in interest rates, foreign exchange rates, equity prices, CPI-indexation and commodity prices. Sources of market risk are imbalances in the Group's balance sheet and open positions in bonds, currencies and equities. Derivative contracts are also potential sources of market risk.

Market risk within the Group can broadly be split into two categories, trading book and banking book. The trading book includes market risk exposures related, directly or indirectly, to the Group's short- and medium-term trading in securities, currencies and other capital market instruments and derivatives. All financial assets and liabilities in the trading portfolio are recognised at fair value and all resulting changes are immediately reflected in the income statement. The banking book includes market risk exposures related to securities held for long-term investment purposes, unlisted securities or holdings in subsidiaries or affiliates. A large part of the banking book market risk is due to mismatches in the composition of assets and liabilities, for example with respect to currencies, interest rates, CPI-indexation or other factors that can affect the Group's earnings or earnings volatility. These mismatches are reported to management and are subject to internal and regulatory limits.

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60. Interest rate risk

Interest rate risk is defined as the current or prospective risk to earnings or capital arising from adverse movements in interest rates. Sensitivity measures like Basis Point Value (BPV) are used to measure and manage risk arising from its fixed income exposures. The BPV measures the effect of a 0.01 percentage point upward parallel shift in the yield curve on the fair value of these exposures.

Interest rate risk in the trading book

The fixed income trading unit invests mainly in government bonds, bonds issued by the Housing and Construction Authority which are guaranteed by the Icelandic Government, domestic municipality bonds, and covered bonds issued by other Icelandic banks. Bonds and bills in the Group's liquidity portfolio are also categorised in the trading book. In the following table the total market value (MV) of long and short positions may not be the same as reported in Note 19 since netting between short and long positions is not applied here.

	31.12.2020			31.12.2019		
Trading bonds and debt instruments, long positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	4,103	1.87	(0.77)	1,143	6.84	(0.78)
Non-indexed	86,829	0.66	(5.70)	31,855	0.41	(1.29)
Total	90,932	0.71	(6.47)	32,998	0.63	(2.07)

	31.12.2020			31.12.2019		
Trading bonds and debt instruments, short positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	224	6.00	0.12	150	6.00	0.10
Non-indexed	351	5.00	0.17	615	4.00	0.28
Total	575	5.39	0.29	765	4.39	0.38
Net position of trading bonds and debt instruments	90,357	0.68	(6.18)	32,233	0.54	(1.69)

The following table shows the interest rate sensitivity of the Group's trading book from a parallel 100 basis points change in all yield curves.

Sensitivity analysis for trading bonds and debt instruments		31.12.2020		31.12.2019	
		Effect on profit or (loss)			
Currency	Parallel shift in yield curve (basis points)	Downward shift	Upward shift	Downward shift	Upward shift
ISK, indexed	100	78	(78)	87	(87)
ISK, non-indexed	100	393	(393)	44	(44)
EUR	100	108	(108)	40	(40)
USD	100	12	(12)	32	(32)
Other total	100	61	(61)	9	(9)
Total		652	(652)	212	(212)

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Interest rate risk in the banking book

Interest rate risk in the banking book arises from the Group's core banking activities. The main source of this type of interest rate risk is the risk of loss from fluctuations in future cash flows or fair value of financial instruments as interest rates change over time, reflecting the fact that the Group's assets and liabilities are of different maturities and are priced relative to different interest rates.

The following table shows the interest sensitivity of the Group's banking book from a parallel 100 basis points change in all yield curves, with all other variables held constant, categorised by the date of next interest rate reset.

Sensitivity analysis for interest rate risk in the banking book

At 31 December 2020

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	-	(108)	236	(2,554)	4,388	(1,232)	730
ISK, non-indexed	(13)	(28)	(43)	(945)	(218)	(4)	(1,251)
EUR	60	(58)	(34)	123	-	(1)	90
SEK	(5)	-	-	-	-	-	(5)
USD	27	-	-	-	-	(1)	26
Other	(2)	(12)	-	(8)	-	(6)	(28)
Total	67	(206)	159	(3,384)	4,170	(1,244)	(438)

At 31 December 2019

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	55	60	(442)	(1,668)	1,995	193	193
ISK, non-indexed	7	(12)	11	89	(10)	(9)	76
EUR	(17)	(20)	(29)	118	-	(2)	50
SEK	10	-	-	-	-	-	10
USD	(42)	-	-	-	-	(1)	(43)
Other	12	(11)	-	41	-	(6)	36
Total	25	17	(460)	(1,420)	1,985	175	322

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61. Currency risk

Currency risk is the risk that earnings or capital may be negatively affected from the fluctuations of foreign exchange rates, due to transactions in foreign currencies or due to a mismatch in the currency composition of assets or liabilities.

The analysis of the Group's foreign currency exposure presented below is based on the contractual currency of the underlying balance sheet items. Additionally, there are off-balance sheet items that carry currency risk and are included in the total currency imbalance. The off-balance sheet amounts below represent the notional amounts of derivatives and unsettled spot agreements.

Series C preferred shares in Visa Inc., which the Group holds, are included in the currency imbalance even though the shares are classified as held for sale.

Currency analysis at 31 December 2020

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	779	281	148	45	17	54	56	101	31	119	1,631
Loans to credit institutions	28,586	44,519	1,301	422	248	880	9,487	415	375	100	86,333
Bonds and debt instruments	25,052	3,932	7	-	-	3,894	11,195	-	-	-	44,080
Loans to customers	127,317	31,584	1,160	521	3,330	84	3,215	2,788	7,468	29	177,496
Shares and equity instruments	32	1,551	338	-	-	152	32	-	-	-	2,105
Other assets	606	124	-	-	-	34	-	-	3	-	767
Total assets	182,372	81,991	2,954	988	3,595	5,098	23,985	3,304	7,877	248	312,412
Liabilities											
Deposits from credit institutions	10,958	788	23	-	-	-	1	-	-	-	11,770
Deposits from customers	26,757	30,607	3,917	517	386	1,017	3,132	2,277	392	20	69,022
Derivative instruments and short positions	-	-	-	-	-	9	-	-	-	-	9
Debt issued and other borrowed funds	143,255	-	-	-	-	38,589	21,169	-	-	-	203,013
Subordinated loans	-	-	-	-	-	27,194	-	-	-	-	27,194
Other liabilities	415	114	-	-	-	19	-	29	1	-	578
Total liabilities	181,385	31,509	3,940	517	386	66,828	24,302	2,306	393	20	311,586
Net on-balance sheet position	987	50,482	(986)	471	3,209	(61,730)	(317)	998	7,484	228	826
Net off-balance sheet position	463	(46,840)	920	(484)	(3,198)	61,672	268	(829)	(7,468)	(276)	4,228
Net position	1,450	3,642	(66)	(13)	11	(58)	(49)	169	16	(48)	5,054

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Currency analysis at 31 December 2019

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	942	319	210	52	24	51	73	114	58	123	1,966
Loans to credit institutions	11,689	25,740	1,650	378	534	116	9,707	1,294	272	687	52,067
Bonds and debt instruments	12,930	10,937	3	-	-	-	8,232	-	-	-	32,102
Loans to customers	112,185	29,486	2,037	581	3,185	3	3,408	635	6,005	33	157,558
Shares and equity instruments	31	3,371	419	-	-	-	27	-	-	-	3,848
Other assets	390	1,866	338	6	-	73	2	20	-	458	3,153
Total assets	138,167	71,719	4,657	1,017	3,743	243	21,449	2,063	6,335	1,301	250,694
Liabilities											
Deposits from credit institutions	9,145	558	1	-	-	-	-	-	-	-	9,704
Deposits from customers	32,247	27,939	3,810	385	395	874	3,317	3,617	453	42	73,079
Debt issued and other borrowed funds	91,809	-	-	-	-	37,768	19,565	-	-	-	149,142
Subordinated loans	-	-	-	-	-	22,674	-	-	-	-	22,674
Other liabilities	1,728	944	558	35	3	162	5	47	2	665	4,149
Total liabilities	134,929	29,441	4,369	420	398	61,478	22,887	3,664	455	707	258,748
Net on-balance sheet position	3,238	42,278	288	597	3,345	(61,235)	(1,438)	(1,601)	5,880	594	(8,054)
Net off-balance sheet position	(4,344)	(41,574)	(231)	(610)	(3,345)	61,127	1,255	1,726	(5,840)	(203)	7,961
Net position	(1,106)	704	57	(13)	-	(108)	(183)	125	40	391	(93)

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The following table shows the effect of a 10% depreciation or appreciation of foreign exchange rates where the Group had positions at year-end, with all other variables held constant.

Sensitivity analysis for currency risk	31.12.2020		31.12.2019	
	Effect on profit or (loss)			
Currency	-10%	10%	-10%	10%
EUR	(145)	145	111	(111)
USD	(364)	364	(70)	70
GBP	7	(7)	(6)	6
CHF	1	(1)	1	(1)
JPY	(1)	1	-	-
SEK	6	(6)	11	(11)
NOK	5	(5)	18	(18)
DKK	(17)	17	(13)	13
CAD	(2)	2	(4)	4
Other foreign currencies	5	(5)	(39)	39
Total	(505)	505	9	(9)

62. Shares and equity instruments

The Group's equity exposure in the trading book arises from flow trading and market making with shares listed on the Nasdaq Iceland Stock Exchange. Shares and equity instruments in the banking book are classified as mandatorily at fair value through profit or loss or are classified as held for sale.

The following table shows how a 10% shift in equity prices would affect the Group's equity and net financial income. Securities used for hedging are excluded.

Sensitivity analysis for shares and equity instruments		31.12.2020		31.12.2019	
		Effect on profit or (loss)			
Portfolio	Change in equity prices	Downward shift	Upward shift	Downward shift	Upward shift
Trading book	10%	(113)	113	(169)	169
Banking book	10%	(462)	462	(806)	806
Total		(575)	575	(975)	975

63. Inflation risk

The Group is exposed to inflation risk since the value of CPI-linked assets exceeds CPI-linked liabilities. The value of these assets and liabilities changes according to changes in the CPI at any given time and all changes in the CPI affect profit and loss. A 1% increase in the index would lead to an ISK 262 million increase in the balance sheet and a 1% decrease would lead to a corresponding decrease, other risk factors held constant.

The off-balance sheet position of certain derivatives were incorrect in the year-end 2019 figures. Off-balance sheet liabilities positions have consequently been adjusted downwards by ISK 11,400 million. The year-end 2019 CPI imbalance therefore increased from ISK 9,260 million to ISK 20,660 million.

	31.12.2020	31.12.2019
Bonds and debt instruments	4,684	2,103
Loans to customers	268,062	295,725
Total CPI-linked assets	272,746	297,828

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63. Cont'd

	31.12.2020	31.12.2019
Deposits from customers	90,353	98,766
Debt issued and other borrowed funds	136,487	125,975
Off-balance sheet position	19,725	52,427
Total CPI-linked liabilities	246,565	277,168
CPI imbalance	26,181	20,660

64. Derivatives

The Group uses derivatives to hedge currency exposure, interest rate risk in the banking book as well as inflation risk. However, the Group is subject to indirect exposure through customers' margin trading. Margin trading is subject to continuous monitoring and collateral requirements. Other derivatives held for trading or for other purposes are insignificant.

65. Capital management

The following tables show the capital base, risk exposure amount, the resulting capital ratios, and leverage for the Group at 31 December 2020 and 31 December 2019.

The Group's regulatory capital requirement is calculated according to CRD IV as implemented through Act no. 161/2002 on Financial Undertakings and regulation no. 233/2017 on prudential requirements for financial undertakings. Capital requirement calculations for credit risk and market risk are based on the standardised approach whereas the capital requirement calculations for operational risk are based on the basic indicator approach.

Article 501 of the capital requirements regulation (EU) no. 575/2013 of the European Parliament came into effect in Iceland on 1 January 2020. This article stipulates capital requirements deduction for credit risk on exposures to SMEs and lowers the risk exposure amount by ISK 13.7 billion as of 31 December 2020, corresponding to a 30 basis point increase in the Group's capital ratio.

EU regulation no. 2017/2395 regarding transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds, was ratified into Icelandic law in May 2020. The regulation allows for the phasing in of capital impacts due to IFRS 9, allowing institutions to include a predefined level of provisions as part of CET1 capital. Íslandsbanki has elected to make use of the transitional arrangements, which will add ISK 5.1 billion to CET1, corresponding to an increase of 55 basis points in the Group's capital ratio.

The Group aims at managing its capital position and the corresponding capital ratios above the overall regulatory capital requirement. According to the latest SREP report from the Financial Supervisory Authority of the Central Bank, applicable as of 22 September 2020, the overall capital requirement is 17.0%. The Group's capital target includes a 0.5-2.0% management buffer on top of the overall capital requirement.

The minimum leverage ratio for Icelandic financial institutions is 3%.

	31.12.2020	31.12.2019
CET1 capital		
Ordinary share capital	10,000	10,000
Share premium	55,000	55,000
Reserves	6,181	7,065
Retained earnings	113,529	105,569
Non-controlling interests	1,494	2,428
IFRS 9 reversal due to transitional rules	5,164	-
Fair value changes due to own credit standing	238	392
Tax assets	(259)	(476)
Intangible assets	(3,478)	(4,330)
Total CET1 capital	187,869	175,648

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65. Cont'd

	31.12.2020	31.12.2019
Tier 2 capital		
Qualifying subordinated loans	27,194	22,674
Total capital base	215,063	198,322
Risk exposure amount		
- due to credit risk	830,141	789,180
- due to market risk	16,626	7,919
Market risk, trading book	11,306	6,488
Currency risk	5,320	1,431
- due to credit valuation adjustment	1,728	2,027
- due to operational risk	85,026	85,424
Total risk exposure amount	933,521	884,550
Capital ratios		
Tier 1 ratio	20.1%	19.9%
Total capital ratio	23.0%	22.4%
Leverage ratio		
Exposure amount		
On-balance sheet exposures	1,333,807	1,189,062
Off-balance sheet exposures	41,067	38,849
Derivative exposures	9,922	9,461
Leverage ratio total exposure measure	1,384,797	1,237,372
Tier 1 capital	187,869	175,648
Leverage ratio	13.6%	14.2%

66. Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. The Group's definition of operational risk includes reputational risk, legal risk, model risk, conduct risk and compliance risk among other risk factors.

The ultimate responsibility for ensuring an adequate operational risk management and internal control framework at Íslandsbanki lies with the Board of Directors. The Board has approved an Operational Risk Policy which outlines the Bank's framework for operational risk management. Risk Management is responsible for implementing the Bank's operational risk framework, for developing, maintaining the Operational Risk Policy and for communicating the policy to the Bank's employees.

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Notes to the Consolidated Financial Statements

67. Significant accounting policies

The accounting policies set out below have been applied consistently by the Group for the periods presented in these consolidated financial statements.

67.1 Basis of consolidation

The consolidated financial statements of the Group comprise the financial statements of Íslandsbanki hf., as the parent company, and its subsidiaries. The Group consolidates its subsidiaries on the basis of control.

Control

Subsidiaries are investments that the Group has control over. The Group controls an investment when the Group is exposed, or has rights, to variable returns from its involvement with the investment and has the ability to affect those returns through its power over the investment. The Group has power over an entity when the Group has existing rights that give it the current ability to direct the relevant activities and the ability to exercise its right.

Generally, there is a presumption that a majority of voting rights results in control. However, in individual circumstances, the Group may still exercise control with less than 50% shareholding, or may not be able to exercise control with over 50% of an entity's shares.

When assessing whether the Group has power over the investment and therefore controls the variability of this return, the Group considers all relevant facts and circumstances, including the contractual arrangements with the other vote holders of the entity, rights arising from other contractual arrangements, the Group's voting rights and potential voting rights.

The Group reassesses its control over subsidiaries on a regular basis.

Business combinations

The Group accounts for each business combination by applying the acquisition method. Under the acquisition method, the Group identifies itself as the acquirer, determines the acquisition date, recognises and measures the identifiable assets acquired, the liabilities assumed and any non-controlling interests in the acquiree, and recognises and measures any goodwill or gain from a bargain purchase.

Consolidation

Consolidation of a subsidiary begins when the Group obtains control of the subsidiary and ceases when the Group no longer has control of the subsidiary.

In preparing the consolidated financial statements, Íslandsbanki combines its financial statements with those of its subsidiaries, line by line, by adding together like items of assets, liabilities, equity, income, expenses and cash flows. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with the Group's accounting policies. All intra-group balances, income and expenses relating to transactions between group entities are eliminated in full on consolidation. This also applies to subsidiaries classified as disposal groups held for sale (see Note 67.11).

A change in the Group's ownership interest in a subsidiary, without a loss of control, is accounted for as an equity transaction.

Non-controlling interests

Non-controlling interests represent equity in subsidiaries not attributable, directly or indirectly, to the Group.

For each business combination the Group measures non-controlling interests, at the acquisition date, at either fair value or their proportionate share of the acquiree's identifiable net assets.

The Group presents non-controlling interests within equity in the statement of financial position, separately from the equity attributable to equity holders of Íslandsbanki. Profit or loss and each component of other comprehensive income are attributed to equity holders of Íslandsbanki and to non-controlling interests even if this results in the non-controlling interests having a deficit balance. This also applies to subsidiaries classified as disposal groups held for sale.

Loss of control

If the Group loses control of a subsidiary, it derecognises the related assets, liabilities, non-controlling interests and other components of equity, while any resultant gain or loss is recognised in profit or loss in the line item "Other operating income", or in the line item "Discontinued operations, net of income tax" if the subsidiary is classified as disposal group held for sale.

Any investment retained by the Group in the former subsidiary is recognised at its fair value at the date when control is lost.

Notes to the Consolidated Financial Statements

67.1 Cont'd

Funds management

The Group acts as a manager for Undertakings for Collective Investment in Transferable Securities (UCITS) and investment funds as well as other funds for collective investment that accept capital from investors. Such funds are financed by issuing unit share certificates or shares. The Group does not have any contractual financial responsibility with respect to such custom units. The funds are not consolidated unless they are under the control of the Group.

The Group reviews all the facts and circumstances in order to decide if these funds should be consolidated. The Group is deemed to be a principal and hence controls and consolidates the funds, when it acts as fund manager and cannot be removed without cause, has variable returns through significant unit holdings and/or guarantee, and is able to influence the returns of the funds by exercising its power.

67.2 Investments in associates

Associates are entities over which the Group has significant influence to participate in the financial and operating policy decisions of an entity but does not have control over those policies. It is presumed that the Group has significant influence if the Group holds 20-50% of the voting power of an entity. Considerations made in determining significant influence are similar to those used to determine control over subsidiaries (see Note 67.1).

The Group accounts for its investments in associates using the equity method. Under the equity method, investments in associates are initially recognised at cost. After the acquisition date the carrying amount of each investment is adjusted to recognise changes in the Group's share of net assets. Distributions received from an associate reduce the carrying amount of the investment. If goodwill is in place related to acquisitions of associates then it is included in the carrying amount of the investments and is not tested for impairment separately.

The consolidated financial statements of the Group include the Group's share of the profit or loss and other comprehensive income of associates, from the date that significant influence commences until the date that significant influence ceases.

When the Group's share of losses of an associate exceeds its interest in the associate, the carrying amount of that associate is reduced to nil and recognition of further losses is discontinued, except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate. If the associate subsequently reports profits, the Group resumes recognising its share of profits only after its share of profits equals the share of losses not recognised.

After application of the equity method, the Group determines whether it is necessary to recognise an impairment loss on its investments in associates. At each reporting date, the Group determines whether there is objective evidence that individual investments in associates are impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying amount, and the impairment loss is recognised in profit or loss.

Upon loss of significant influence over an associate, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognised in profit or loss in the line item "Other operating income".

Income and expenses from investments in associates are recognised in profit or loss in the line item "Other operating income".

67.3 Foreign currencies

The financial statements of each of the Group's entities are measured using the functional currency of the respective entity.

Foreign currency transactions

On initial recognition transactions in foreign currencies are translated into functional currencies at the spot exchange rate at the date of the transactions. At the end of each reporting period monetary assets and liabilities denominated in foreign currencies are retranslated into functional currencies using the closing rate. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated into the functional currency using the exchange rate at the date when the fair value was determined.

All foreign currency differences arising on currency translation from one currency to another are recognised in profit or loss in the line item "Net foreign exchange gain (loss)".

67.4 Financial assets and financial liabilities

Recognition

The Group recognises a financial asset and a financial liability in its statement of financial position on the trade date, which is the date on which the Group becomes party to the contractual provisions of the instrument, except for loans which are recognised on the date when cash is advanced by the Group to the borrowers. At initial recognition, the Group measures a financial asset or a financial liability at its fair value plus, in the case of a financial asset or a financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or the financial liability.

Derecognition

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

The Group derecognises financial assets in the following circumstances:
• When the contractual rights to the cash flows from the financial assets expire, or
• When the Group transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which:
- The Group transfers substantially all the risks and rewards of ownership of the financial assets, or
- The Group neither transfers nor retains substantially all the risks and rewards of ownership of the financial assets and it does not retain control of the financial assets.

Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

The Group enters into transactions whereby it transfers assets recognised in its statement of financial position, but retains either all or substantially all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised from the statement of financial position of the Group. Transfers of assets with retention of all or substantially all risks and rewards include, for example, repurchase transactions and securities lending.

The Group does not derecognise from its statement of financial position securities which the Group sells under agreements to repurchase at a specified future date ("repos") at a fixed price or at the sale price plus a lender's return. The Group recognises the cash received as a liability in its statement of financial position. The difference between the sale and repurchase prices is recognised as interest expense over the life of the agreement using the effective interest method.

Securities lending and borrowing transactions are usually collateralised by securities or cash. The transfer of securities to counterparties is only reflected in the statement of financial position if the risks and rewards of ownership are also transferred. Cash advanced or received as collateral is recorded as an asset or liability.

In transactions in which the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

Modifications

Substantial modifications of terms of existing financial assets, or replacements with new ones with significantly different terms, result in the Group derecognising the original financial assets and recognising new financial assets at fair value.

Classification and measurement of financial assets

For the purpose of measuring its financial assets, the Group classifies them at inception in one of the following categories:
• Financial assets at amortised cost
• Financial assets at fair value through other comprehensive income
• Financial assets at fair value through profit or loss
• Derivative assets held for hedging

The measurement basis of individual financial assets is determined based on an assessment of the cash flow characteristics of the assets and the business models under which they are managed.

The business models

The business models are determined by the Group's key management personnel in the way that assets are managed and their performance is reported to them. The Group determines its business models at a level that reflects the way groups of financial assets are managed together to achieve a particular business objective. This condition is not an instrument-by-instrument approach to classification, but is determined at a higher level of aggregation. The Group's business models fall into the following three categories: Held to collect, Held to collect and for sale, and Other fair value business models, where assets are held for trading or managed on a fair value basis and are neither Held to collect nor Held to collect and for sale.

67.4 Cont'd

Solely payments of principal and interest (SPPI)

Financial assets held within the business models Held to collect and Held to collect and for sale, are assessed to evaluate if their contractual cash flows are comprised of solely payments of principal and interest. SPPI payments are those which are consistent with a basic lending arrangement. Principal is the fair value of the financial asset at initial recognition and changes over the life of the financial asset, for example if there are repayments of principal. Interest relates to basic lending returns, including compensation for the time value of money and credit risk associated with the principal amount outstanding over a period of time. Interest can also include consideration for other basic lending risks (for example, liquidity risk) and costs (for example, servicing or administrative costs), as well as a profit margin that is consistent with a basic lending arrangement.

Where the contractual terms introduce exposure to risk or variability of cash flows that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

Financial assets at amortised cost

A financial asset is classified as being subsequently measured at amortised cost if the contractual terms of the financial asset give rise to cash flows that are solely payments of principal and interest and the asset is held within a business model whose objective is to collect contractual cash flows, i.e. Held to collect.

Financial assets at amortised cost are measured using the effective interest method. Amortised cost is calculated by taking into account the amount at which the assets are measured at initial recognition less principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount (such as due to discounts or premiums on acquisition and fees and costs that are an integral part of the effective interest rate), and minus any reduction for impairment. Accrued interest is included in the carrying amount of the financial asset in the statement of financial position. Impairment losses and reversals of impairment losses are recognised in profit or loss in the line item "Net impairment on financial assets".

Financial assets at fair value through other comprehensive income (FVOCI)

For shares and equity instruments that are not held for trading, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses, including any related foreign exchange component, in other comprehensive income rather than profit or loss. This election is made on an instrument-by-instrument basis. Shares and equity instruments at FVOCI are not subject to an impairment assessment. Dividends are to be presented in profit or loss, as long as they represent a return on investment. On derecognition there is no recycling of fair value gains and losses to profit or loss.

Financial assets at fair value through profit or loss (FVTPL)

Financial assets classified at fair value through profit or loss are all other financial assets which are not classified at amortised cost or at fair value through other comprehensive income. This includes financial assets classified mandatorily at fair value through profit or loss and financial assets which are irrevocably designated by the Group at initial recognition as at fair value through profit or loss that would otherwise meet the requirements to be measured at amortised cost or at FVOCI. The Group designates financial assets as at fair value through profit or loss if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise. During the year the Group did not classify any financial assets as designated at fair value through profit or loss.

Financial assets at fair value through profit or loss are initially recognised and subsequently measured at fair value in the statement of financial position. Changes in fair value are recognised in profit or loss in the line item "Net financial income (expense)", except for interest earned, which is recognised in the line item "Interest income" and foreign exchange gains and losses, which are included in the line item "Net foreign exchange gain (loss)".

Derivative assets held for hedging

Derivative assets held for hedging consist of derivatives with positive fair value which are designated and accounted for as hedging instruments (see Note 67.7).

Classification and measurement of financial liabilities

For the purpose of measuring its financial liabilities, the Group classifies them at inception in one of the following categories, except for loan commitments and financial guarantees (see Note 67.12):

- Financial liabilities at amortised cost
- Financial liabilities mandatorily at fair value through profit or loss
- Financial liabilities designated as at fair value through profit or loss
- Derivative liabilities held for hedging

67.4 Cont'd

Financial liabilities at amortised cost

Financial liabilities at amortised cost are non-derivative financial liabilities. Financial liabilities at amortised cost include deposits, debt issued and other borrowed funds, and subordinated loans.

Financial liabilities at amortised cost are recognised initially at fair value net of transaction costs incurred, and subsequently are carried at amortised cost using the effective interest method. Amortised cost is calculated by taking into account the amount at which the financial liabilities are measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount (such as due to discounts or premiums and fees and costs that are an integral part of the effective interest rate). Accrued interest is included in the carrying amount of the liabilities in the statement of financial position.

The amortised cost of certain bonds issued by the Group, which are designated as hedged items in qualifying fair value hedge relationships, is adjusted for changes in the fair value of the bonds attributable to interest rate risk (see Note 67.7).

Financial liabilities mandatorily at fair value through profit or loss

Financial liabilities mandatorily at fair value through profit or loss are financial liabilities incurred principally for the purpose of generating profits from short-term price fluctuations or from the dealer's margin. Financial liabilities mandatorily at fair value through profit or loss consist of short positions in listed bonds and derivatives with negative fair value which are not classified as financial guarantees or are not designated as hedging instruments.

Financial liabilities mandatorily at fair value through profit or loss are initially recognised and subsequently measured at fair value in the statement of financial position. Changes in fair value are recognised in profit or loss in the line item "Net financial income (expense)", except for interest incurred, which is recognised as "Interest expense" on an accrual basis and foreign exchange gains and losses which are included in the line item "Net foreign exchange gain (loss)".

Financial liabilities designated as at fair value through profit or loss

Financial liabilities designated as at fair value through profit or loss are recognised at fair value and changes in fair value attributable to changes in the credit risk of those liabilities are recognised in other comprehensive income and are not subsequently reclassified to profit or loss. The remaining fair value changes are included in profit or loss in the line item "Net financial income (expense)", except for interest incurred, which is recognised as "Interest expense" using the contractual interest rate and foreign exchange gains and losses which are included in the line item "Net foreign exchange gain (loss)".

The Group calculates the fair value attributable to changes in credit risk as the difference between the changes in fair value of the financial liability and the amount of changes in fair value attributable to changes in market interest rates. The change in fair value attributable to changes in market interest rates on financial liabilities is calculated by discounting contractual cash flows at the end of the period with the discount rate of the appropriate market interest rate.

Upon initial recognition, the Group determines if the recognition of gains and losses in other comprehensive income creates or enlarges an accounting mismatch in profit or loss, if applicable the whole fair value change is presented in profit or loss.

Derivative liabilities held for hedging

Derivative liabilities held for hedging consist of derivatives with negative fair value which are designated and accounted for as hedging instruments (see Note 67.7).

Reclassification

Financial assets are reclassified between measurement categories if the objective of the business model in which the financial assets are held changes after initial recognition and if the change is significant to the Group's operations.

Financial liabilities are not reclassified.

Determination of fair value

The fair value of a financial instrument is the transaction price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

When available, the Group measures the fair value of financial assets and financial liabilities using quoted prices in an active market for that instrument. A market is considered active if quoted prices are readily and regularly available and those prices represent actual and regularly occurring transactions. The fair value is based on the most recent observed market prices at the reporting date.

67.4 Cont'd

If a market for a financial instrument is not active, the Group establishes its fair value using a valuation technique. Valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which observable market prices exist, Black-Scholes option pricing models and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index prices and expected price volatilities and correlations. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Group and the counterparty where appropriate.

Periodically, the Group tests the valuation techniques and calibrates against historical data and using prices from observable current market transactions for the same instrument, or based on other available observable market data.

Changes in the fair value of financial assets and financial liabilities are recognised in profit or loss in the line item "Net financial income (expense)".

The Group has an established control framework with respect to the measurement of fair values. The business unit owning the positions is responsible for their valuations and for submitting the valuation to the Bank's Investment Committee for approval. Risk Management provides an independent review of the results, the valuation methods used and of the use of significant unobservable inputs. The final decision on the validity of the valuation is in the hands of the Bank's Investment Committee.

Impairment of financial assets

The impairment model of IFRS 9 is forward-looking and impairment under IFRS 9 should reflect a probability weighted average of possible outcomes. In addition, the expected credit loss model in IFRS 9 employs a dual measurement approach, under which the loss allowance for expected credit losses (ECL) is measured at each reporting date as either 12-month expected credit losses or lifetime expected credit losses, depending on whether there has been a significant increase in credit risk (SICR) of the financial instrument since initial recognition. To satisfy the provisions of the IFRS 9 standard, a significant amount of modelling must be involved. The models which the Group uses for the calculation of the impairment amount are developed according to the Group's modelling framework. This framework imposes structure on the initial model development work, the model documentation including educational material as needed for users, the approval process for models, the implementation of models and the lifetime support for models, including validation and back-testing. The Group's impairment process, which encompasses all the steps needed to derive the appropriate impairment allowance for each accounting period, is documented and approved by the All Risk Committee.

Stage assignment

At each reporting date, all assets subject to the impairment methodology must be divided into three groups, termed "Stages", reflecting the extent of credit deterioration since initial recognition. This division then has an effect on how the impairment is measured and how interest is recognised.

Stage 1

All assets that have not experienced an SICR are assigned to Stage 1. For these assets, an impairment allowance is recognised which is equal to the expected credit loss arising from credit events occurring within 12 months of the reporting date (12- month ECL). Interest is recognised on the gross carrying amount of the assets.

Stage 2

Assets that the Group determines to have experienced an SICR, but are not credit-impaired, are classified as Stage 2. For these assets, an impairment allowance is recognised which is equal to the expected credit loss arising from all credit events occurring within the expected lifetime of the assets (lifetime ECL). Interest is recognised on the gross carrying amount of the assets.

The Group's definition of an SICR is on the level of an individual asset. The Group assesses that there has been a significant increase in credit risk of an asset if the probability of a credit impairment event, i.e. transfer to Stage 3, occurring over the lifetime of the asset has increased significantly from the origination of the assets. For this purpose, origination does not refer to any modification events which have not resulted in derecognition of the asset. The assessment is based on a defined set of triggers. This includes, as a backstop, the trigger that the asset is more than thirty days past due. Other triggers are internal assessments of outlook, events such as forbearance events which are less severe than a credit event, external credit related information and a significant deterioration in risk assessment compared with the risk assessment done in relation to the origination of the asset. The definition of SICR depends only on the probability of a credit event occurring, it does not take into account collateralisation or any other information related to the expected loss arising from the event. As soon as all triggers for Stage 2 for a particular asset are no longer activated then the asset moves back to Stage 1. Additionally, assets are classed as forborne for two years after a forbearance event has occurred, but forbearance events only cause assets to be in Stage 2 for twelve months and then they migrate back to Stage 1 unless other triggers apply.

67.4 Cont'd

The Group does not employ the low credit risk exemption in the Stage assignment process. In alignment with its operating procedures, the Group has chosen as its accounting policy to measure the impairment allowance for lease receivables at an amount equal to the lifetime ECL only for those assets which have an SICR or are credit-impaired. For other lease receivables the impairment allowance is equal to the 12-month ECL.

Stage 3

This Stage is for assets which are credit-impaired according to the Group's assessment. These assets are therefore experiencing an ongoing credit event. Thus, the 12-month ECL and lifetime ECL are the same amount and this amount is recognised as impairment allowance. For assets in this Stage, interest is recognised on the net carrying amount of assets, i.e. net of impairment allowance.

The Group's definition of being credit-impaired is on a customer level, rather than on the level of an individual asset. According to the definition, a customer is credit-impaired when either of the following holds:

a) The Group assesses that it is unlikely that the customer can service all of their commitments to the Group in accordance with the terms of the agreements without recourse to default provisions in the agreements, or

b) The customer is more than 90 days past due on any of their commitments

The assessment in point a) is made based on a defined set of triggers, which includes serious breach of covenants, serious registrations on an internal watchlist, initiation of serious collection actions and serious external credit related information.

Furthermore, there is a defined set of conditions which must be satisfied so that customers that have been assessed as being credit-impaired are no longer subject to this assessment. This includes probation periods and a view to the future outlook of the customer.

Expected credit loss (ECL)

The ECL for each asset is calculated using models for the probability of a credit impairment event occurring (PD), the loss percentage expected in case of such an event (LGD) and the outstanding amount at the time of the event (EAD). In its simplest form the ECL can be calculated as the product of these factors, however, for several reasons, the actual formula must be more complicated than this.

The Group uses the standardised approach for regulatory capital purposes but has used PD models and LGD models for risk management purposes for several years. These models have been adapted for IFRS 9 purposes. For EAD, and for LGD to a certain extent, new models have been developed.

The PD models are either fully automated statistical models, expert models or hybrid. For the models with a component involving expert input there is a process in place to ensure proper review of the model outcome and periodic reassessment of obligors. The inputs into the models include demographic variables, information from financial statements and past payment behaviour, among other variables.

The effects of the economy on the PD is accounted for with the use of scaling factors which map through-the-cycle PD values to point-in-time PD values. The Group has a model to predict these scaling factors based on an economic forecast. The economic forecast is provided by the Group's Chief Economist. The forecast predicts a range of macroeconomic indicators over a horizon of five years. The model is applied to a subset of these indicators and produces a set of scaling factors. The scaling factors are then reviewed by the All Risk Committee with respect to all of the indicators and any other relevant information available and the committee approves their use for the calculation of the impairment. This process is carried out at least quarterly.

The Group uses three economic scenarios. In addition to the base forecast, scaling factors are produced for a bull and bear case. This is done in order to represent the whole range of possible future economic developments. The actual impairment allowance is the weighted average of the ECL in these different scenarios.

The All Risk Committee determined that it was appropriate to adjust the weights of the scenarios due to the COVID-19 pandemic, generally the scenarios are weighted 25%-50%-25% (good, base, bad) but it was determined appropriate to set the weights at 15%-55%-30%, as this would best represent the probability-weighted average over all possible scenarios.

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67.4 Cont'd

The table below shows macroeconomic indicators of the Group's Chief Economist's macroeconomic forecast

Change in economic indicators %	2020	2021	2022	2023	2024
Economic growth	(8.6)	3.1	4.7	2.5	2.6
Housing prices in Iceland	2.6	1.5	3.0	4.0	4.0
Purchasing power	3.0	1.1	2.1	2.1	1.6
ISK exchange rate index	11.2	3.1	(1.8)	(2.8)	(1.5)
Policy rate, Central Bank of Iceland	1.5	1.2	2.0	3.0	3.5
Inflation	2.7	2.7	1.9	1.9	2.4
Capital formation	(10.2)	1.5	6.7	1.2	3.5
thereof capital formation in industry	(16.9)	(0.2)	8.7	3.5	3.0

The LGD model considers several scenarios for how a facility may develop once a credit event has occurred. One possibility is that the facility cures without a loss. If not, the recoveries may be based on the seizing of collateral and to estimate such recoveries, several scenarios for the development of the value of the collateral are considered. Finally, there may be recoveries even though a formal collateral is not in place. These different recovery scenarios are weighted differently depending on the economic scenario under consideration. This leads to a non-linear interaction and thus a difference between the probability weighted average ECL and the ECL in the most likely scenario.

For EAD it is necessary to account for expected prepayments on term loans and for the expected utilisation of commitments such as credit cards, overdrafts, financial guarantees and credit lines. The expected lifetime of agreements may also extend beyond the contractual lifetime for contracts which are generally extended.

Temporary changes have been made to the impairment model due to COVID-19 pandemic those changes are described in Note 3.

Write-off policy
When the Group has no reasonable expectations of recovering a credit exposure or when it is uneconomical to pursue legal collection, the financial asset is written off. A write-off does not change the debt obligation which is therefore still subject to enforcement activity. Any recoveries of amounts previously written off are credited to the income statement.

The impairment process
In the Group's impairment framework, the Stage assignment and ECL for each financial asset is calculated from the aforementioned models. The outcome is reviewed by the business units and they can propose changes if they provide sufficient supporting material. The impairment and any proposals for changes are reviewed by an Impairment Council appointed by the All Risk Committee and the impairment allowance is approved by the All Risk Committee on a quarterly basis.

The principle of materiality applies to the above discussion on impairment, whereby exceptions related to non-materiality and immaterial adjustments are not discussed.

67.5 Cash and cash equivalents

Cash and cash equivalents are carried at amortised cost in the statement of financial position and at the reporting date the expected credit loss is considered to be low. Impairment losses and reversals of impairment losses are recognised in profit or loss in the line item "Net impairment on financial assets".

Cash and cash equivalents in the statement of cash flows consist of cash on hand, balances with the Central Bank, demand deposits with credit institutions, and short-term loans to credit institutions. Cash and cash equivalents comprise balances with less than three months maturity from the date of acquisition.

67.6 Derivative financial instruments

Derivatives are primarily used in trading activities but are also used to manage the Group's exposure to various risks, such as interest rate risk, inflation risk and currency risk. Derivatives are classified as financial assets or financial liabilities, measured at fair value and presented in the statement of financial position in separate line items as assets or liabilities, depending on whether their fair value at the reporting date is positive (assets) or negative (liabilities).

67.6 Cont'd

The Group applies hedge accounting. Accordingly, some of the Group's derivative financial assets and financial liabilities are accounted for as financial assets or financial liabilities mandatorily at fair value through profit or loss while others are accounted for as derivative assets or liabilities held for hedging (see Note 67.4 and Note 67.7).

When derivatives are embedded in other financial instruments or host contracts, such combinations are known as hybrid instruments with the effect that some of the cash flows of a hybrid instrument vary in a way similar to a stand-alone derivative. These embedded derivatives are measured and presented in the consolidated financial statements as if they were free-standing derivatives. The Group accounts for an embedded derivative separately from the host contract when, the host contract is not an asset in the scope of IFRS 9, is not carried at fair value through profit or loss, the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract, and the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract. When the Group is required to separate and account for embedded derivatives as if they were stand-alone contracts, the Group presents the fair value of the embedded derivatives in the statement of financial position in the same line items in which the Group presents the related host contracts.

67.7 Hedge accounting

The Group elected, as a policy choice permitted under IFRS 9, to continue to apply hedge accounting in accordance with IAS 39.

On initial designation of the hedges, the Group formally documented the relationship between the hedging instruments and hedged items, including the risk management objective and strategy in undertaking the hedge, together with the method that will be used to assess the effectiveness of the hedging relationships. The Group makes an assessment, both at inception of the hedge relationships and on an ongoing basis, of whether the hedging instruments are expected to be highly effective in offsetting the changes in the fair value of the hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within the range of 80-125%. In the assessment the Group assumes that the benchmark interest rate is not altered as result of the transition to alternative benchmark interest rates (see Note 4).

The Group applies fair value hedge accounting with respect to designated hedging relationships consisting of certain fixed-rate euro denominated bonds issued by the Group as the hedged items and certain euro denominated interest rate swaps as the hedging instruments, whereby the Group pays floating rate interest and receives fixed rate interest. The hedging relationships are designated and accounted for as fair value hedges because the interest rate swaps are hedging the exposure of the Group to changes in the fair value of the bonds arising from changes in interest rates. The Group recognises the changes in the fair value of the interest rate swaps immediately in profit or loss together with the changes in the fair value of the bonds which are attributable to the interest rate risk. The changes in the clean fair value of the swaps and the bonds are included in the line item “Net financial income (expense)”, the accrued interest on the bonds and the swaps is included in the line item “Interest expense” and foreign exchange gains and losses on the bond are included in the line item "Net foreign exchange gain (loss)".

If a hedging derivative expires or is sold, terminated or exercised, or a hedge no longer meets the criteria for fair value hedge accounting, or the hedge designation is revoked, then hedge accounting for the corresponding hedging relationship is discontinued prospectively. Any adjustment up to the point of discontinuation to a hedged item for which the effective interest method is used is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

67.8 Property and equipment

Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and impairment losses (see Note 67.19). Where parts of an item of property and equipment have different useful lives, those components are accounted for and depreciated as separate items of property and equipment.

Subsequent costs

The Group recognises in the carrying amount of an item of property and equipment the cost of replacing part of such an item when that cost is incurred, if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in profit or loss as incurred.

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67.8 Cont'd

Depreciation
Items of property and equipment are depreciated from the date they are available for use, except for land, which is not depreciated. The depreciable amount of each item of property and equipment is determined after deducting its residual value. Depreciation is recognised in profit or loss in the line item "Other operating expenses" on a straight-line basis over the estimated useful lives of each part of an item of property and equipment.

The depreciation method, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

The estimated useful lives are as follows:

Buildings	50 years
Right-of-use-assets	1-11 years
Fixtures	6-12 years
Equipment	4-5 years
Vehicles	3 years

67.9 Intangible assets

Software
Software acquired by the Group is measured at cost less accumulated amortisation and impairment losses.

Expenditure on internally developed software is recognised as an asset when the Group is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and can reliably measure the costs to complete the development. The capitalised costs include all costs directly attributable to developing the software and capitalised borrowing costs. Internally developed software is carried at capitalised cost less accumulated amortisation and impairment losses.

Subsequent expenditure on software is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Software is amortised on a straight-line basis over its estimated useful live from the date that it is available for use. The amortisation is recognised in profit or loss in the line item "Other operating expenses". The estimated useful life of software is four to ten years.

67.10 Leases

At the inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Group has elected not to separate non-lease components and account for lease and non-lease components of a contract as a single lease component.

The Group as a lessee

The Group applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Group recognises a lease liability and a right-of-use asset at the lease commencement date. The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets. The Group recognises lease payments associated with these leases as an expense on a straight-line basis over the lease term.

Lease liabilities

The lease liability is initially measured at the present value of the lease payments, both fixed and variable, discounted using the entity's incremental borrowing rate. The incremental borrowing rate is the rate of interest the Group would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The incremental borrowing rate is subject to estimation when no observable rates are available. The lease liability is measured at amortised cost using the effective interest method and remeasured when there is a change in future payments, e.g. arising from a change in an index or an assessment of whether extension or termination options will be exercised. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made.

67.10 Cont'd

The lease term is determined by the Group as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised. An assessment of whether the entity will exercise an extension or termination option is made by management annually. If the assessment of whether the Group will exercise an extension or termination option changes after the commencement date the lease liability is remeasured and a corresponding adjustment is made to the carrying amount of the right-of-use asset.

Right-of-use assets

The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred less any lease incentives received. For any remeasurement of the lease liability a corresponding adjustment is made to the carrying amount of the right-of-use asset or recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero. The right-of-use-asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. Right-of-use assets are subject to impairment.

If a lease modification increases the scope of the lease by adding a right to use of one or more underlying assets and the consideration for the lease increases by an amount commensurate with the stand-alone price for the increased scope and any adjustments to the price that reflects the circumstances of the particular contract, then the modification is accounted for as a separate lease. For lease modifications that are not accounted for as separate leases the lease term of the modified lease is redetermined and the lease liability remeasured using the revised lease payments and discounted using the incremental borrowing rate at the effective date of modification. Any adjustment of the lease liability is then correspondingly made to the right-of-use asset.

The Group presents right-of-use assets in the line item "Property and equipment" and lease liabilities in the line item "Other liabilities" in the statement of financial position. Maturity analysis of lease liabilities is disclosed in Note 58. Interest on lease liabilities is recognised in profit or loss in the line item "Interest expense". Depreciation of right-of-use assets is recognised in profit or loss in the line item "Other operating expenses".

The Group as a lessor

The Group classifies leases based on the substance of the arrangements and the extent of the transfer of risks and rewards incidental to ownership of the leased asset. A lease is classified as an operating lease if the lessor does not transfer substantially all the risks and rewards incidental to ownership. A lease is classified as a finance lease if the lessor transfers substantially all the risks and rewards incidental to ownership.

When the Group is the lessor in a capital lease, the Group recognises a receivable equal to the net investment in the lease and presents it in the line item "Loans to customers" in the statement of financial position. The Group applies its accounting policies for derecognition and impairment of financial assets also to its capital lease receivables. The Group recognises the finance income from capital lease receivables in profit or loss in the line item "Interest revenue" over the period of the capital lease so as to give a constant periodic rate of return on the net investment in the capital lease.

When the Group is a lessor in arrangements which involve the legal form of capital leases, but which in substance do not involve leases, the Group classifies them within loans at amortised cost.

67.11 Non-current assets and disposal groups held for sale

Non-current assets and disposal groups are either classified as held for sale when the Group expects to recover their carrying amount principally through a sale transaction rather than through continuing use or as held for distribution to owners when the Group is committed to distribute the asset, or disposal group, to the owners.

For this to be the case, the assets, or disposal groups, must be available for immediate sale, or distribution, in their present condition and their sale, or distribution, must be highly probable. The sale must only by subject to terms that are usual and customary for sales of such assets, or disposal groups.

Non-current assets and disposal groups are presented in a separate line in the statement of financial position but Non-current liabilities and disposal groups are presented in the line item "Other liabilities". Non-controlling interests in a disposal group are presented within equity.

Immediately before the initial classification as held for sale or distribution the assets, or components of disposal groups, are remeasured in accordance with applicable accounting policies. Thereafter, the assets, or disposal groups, are measured at the lower of their carrying amount and fair value less costs to sell or costs to distribute.

Income and expenses of non-current assets and disposal groups held for sale are recognised in profit or loss in the line item "Discontinued operations, net of income tax" (see Note 67.21).

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67.12 Loan commitments and financial guarantees

Loan commitments are firm commitments of the Group to provide credit under pre-specified terms and conditions. Expected credit loss of loan commitments (see Note 67.4) is recognised in the statement of financial position in the line item "Other liabilities". Loan commitment fees received by the Group are recognised in profit or loss in the line item "Fee and commission income".

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Financial guarantees are issued by the Group to credit institutions and other parties on behalf of its customers so that they can secure loans, overdrafts and banking facilities.

Liabilities arising from financial guarantees issued by the Group are initially measured at their fair value, being the premium received. Subsequently the liabilities are carried at the higher of the amount representing the initial fair value of the guarantee and the expected credit loss allowance of the guarantee (see Note 67.4). Any changes in the liabilities arising from financial guarantees are recognised in profit or loss. The premium received is recognised in profit or loss in the line item "Fee and commission income" over the life of the guarantee.

67.13 Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, if it is probable that the Group will be required to settle the obligation with an outflow of resources, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that the reimbursement will be received and the amount of the receivable can be measured reliably.

67.14 Employee benefits

All Group entities are required to pay, on a mandatory and contractual basis, contributions to public and private pension funds. The Group has no further payment obligations once these contributions have been paid. The Group recognises these contributions as salary related expenses when they become due. The Group does not have a defined benefit pension plan.

Short-term employee benefits include salaries, cash bonuses, non-monetary benefits and compensated absences. Short-term employee benefit obligations are expensed by the Group as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

67.15 Equity

Share capital

The share capital disclosed in the consolidated financial statements represents the total nominal value of ordinary shares issued by the Bank. Incremental costs directly attributable to the issuance of ordinary shares are recognised as a deduction from equity, net of any tax effects.

Dividends on shares

Dividends payable to shareholders of the Bank are recognised as a liability and deducted from equity in the period in which the dividends are approved by the shareholders at the Bank's Annual General meeting. Dividends payable to non-controlling shareholders in subsidiaries are recognised as a liability and deducted from equity in the period in which the dividends are approved by the shareholders' meeting of the subsidiaries. Dividends declared after the reporting date are not recognised as a liability at the reporting date.

Statutory reserve

According to the Act on Public Limited Companies no. 2/1995 the statutory reserve shall amount to 25% of the share capital of the Bank.

67.15 Cont'd

Restricted reserves

The Group is to transfer, if applicable, certain amounts from retained earnings to restricted reserves which can therefore not be distributed as dividends to shareholders. These restricted reserves are specified as follows:

Restricted reserve due to capitalised development costs

When the Group capitalises development cost it transfers a corresponding amount from retained earnings to a restricted reserve. In the future the restricted amount is to be transferred back to retained earnings as the capitalised development cost is amortised in profit or loss.

Restricted reserve due to fair value changes of financial assets

The Group transfers fair value changes of financial assets at fair value through profit or loss, net of tax if applicable, from retained earnings to a restricted reserve. Amounts recognised in the reserve are transferred back to retained earnings upon sale of the financial asset.

Restricted reserve due to unrealised profit of associates

If share of profit of an associated company is in excess of dividend received or which can be claimed, the Group transfers the difference to a restricted reserve in equity. If the Group's shareholding in an associate is sold or written off the applicable amount recognised in the reserve is transferred to retained earnings.

Fair value reserve

Fair value reserve comprises all unrealised gains or losses related to fair value changes of equity instruments classified at fair value through other comprehensive income. On derecognition of the equity instruments fair value changes are not reclassified to profit and loss.

Liability credit reserve

Changes in fair value attributable to changes in the credit risk of financial liabilities designated as at fair value through profit or loss are recognised in liability credit reserve. On derecognition the fair value changes are not reclassified to profit or loss.

Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of foreign operations.

67.16 Interest income and interest expense

For all financial assets and financial liabilities measured at amortised cost, interest income and interest expense are recognised in profit or loss using the effective interest method.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, when appropriate, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows, considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation generally includes all fees and amounts paid or received between parties to the contract that are an integral part of the effective interest rate, as well as transaction costs and all other premiums or discounts.

The effective interest rate is established on initial recognition of financial assets and financial liabilities and their carrying amount is subsequently adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate. The change in carrying amount is recorded as interest income or interest expense. For floating rate instruments, interest income or interest expense is generally recognised based on the current market rate plus or minus amortisation or accretion of the discount or premium based on the original effective interest rate.

Interest on impaired financial assets is calculated by applying the original effective interest rate of the financial asset. For financial assets in Stage 1 and Stage 2 interest is recognised on the gross carrying amount of the assets and for financial assets in Stage 3 interest is recognised on the gross carrying amount of the assets, net of impairment allowance (see Note 67.4).

Interest income and interest expense include gains and losses on derecognition of financial assets and financial liabilities measured at amortised cost.

For financial assets and financial liabilities at fair value through profit and loss, interest income and interest expense are recognised through profit or loss on an accrual basis, except for financial liabilities at fair value through profit or loss (see Note 67.4).

Accrued interest on interest rate swaps, which are designated and accounted for as hedging instruments in fair value hedges of the interest rate risk arising from certain fixed-rate euro denominated bonds issued by the Group (see Note 67.7), is recognised in profit or loss as an adjustment to the interest expense recognised for the bonds.

67.17 Net fee and commission income

Fees and commissions are recognised to reflect the transfer of services to customers at an amount that reflects the consideration that is expected to be received for such services. Fee and commission income and expenses that are integral to the effective interest rate on a financial asset or financial liability are included in the measurement of the effective interest rate.

Fees for loan commitments that are likely to be utilised are recognised as an adjustment to the effective interest rate of the loan. When a loan commitment is not expected to be utilised, fees are recognised in profit or loss on a straight-line basis over the commitment period.

Loan syndication fees are recognised as revenue in profit or loss when the syndication has been completed and the Group has retained no part of the loan package for itself or has retained a part at the same effective interest rate as the other participants.

Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as the arrangement of the acquisition of shares or other securities, or the purchase or sale of businesses, are recognised on completion of the underlying transaction.

Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis.

Asset management fees related to investment funds are recognised rateably over the period in which the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continuously provided over an extended period of time. Performance-linked fees or fee components are recognised when the performance criteria are fulfilled.

Where it is assessed that the Group is acting as an agent, the consideration is presented on a net basis.

67.18 Net financial income (expense)

Net financial income (expense) consists of net gain (loss) on financial assets and financial liabilities mandatorily at fair value through profit or loss, net gain (loss) on financial liabilities designated as at fair value through profit or loss and net gain (loss) on fair value hedges.

Net gain (loss) on financial assets and financial liabilities mandatorily at fair value through profit or loss
Net gain (loss) on financial assets and financial liabilities mandatorily at fair value through profit or loss includes all realised and unrealised fair value changes of financial assets and financial liabilities classified by the Group as mandatorily at fair value through profit or loss, except for interest income and interest expense, which are included in the line items "Interest income" and "Interest expense", and foreign exchange gains and losses, which are included in the line item "Net foreign exchange gain (loss)". Dividend income from financial assets is recognised in the income statement when the Group's right to receive payment is established.

Net gain (loss) on financial liabilities designated as at fair value through profit or loss
Net gain (loss) on financial liabilities designated as at fair value through profit or loss includes all realised and unrealised fair value changes of financial liabilities designated by the Group as at fair value through profit or loss, except for changes in fair value attributable to changes in credit risk which is recognised in other comprehensive income, interests incurred which are included in the line item "Interest expense", and foreign exchange gains and losses which are included in the line item "Net foreign exchange gain (loss)".

Net gain (loss) on fair value hedges
Net gain (loss) on fair value hedges includes the changes in the clean fair value of interest rate swaps which are accounted for as hedging instruments in fair value hedges and the changes in the fair value of certain bonds, which are attributable to the interest rate risk of the bonds, and are accounted for as the hedged items in fair value hedges (see Note 67.7).

67.19 Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets, other than deferred tax assets and non-current assets and disposal groups held for sale, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the Group estimates the recoverable amount of the asset. If the carrying amount of an asset exceeds its estimated recoverable amount an impairment loss is recognised in profit or loss.

An impairment loss for non-financial assets is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Notes to the Consolidated Financial Statements

67.20 Taxes

Income tax expense

Income tax expense comprises special financial activities tax, current tax and deferred tax and is disclosed as a separate line item in the income statement. Income tax expense from discontinued operations is included in the income statement in the line item "Discontinued operations, net of income tax" (see Note 67.21). Income tax is recognised in profit or loss, except to the extent that it relates to items recognised directly in equity, consistent with the recognition of the underlying item to which it relates.

Bank tax

Bank tax is calculated as 0.145% (2019: 0.376%) of total liabilities at year-end as determined for tax purposes, in excess of ISK 50,000 million, excluding tax liabilities. The Bank tax is considered a non-deductible expense for the calculation of income tax. The Bank tax is shown in a separate line in the income statement and is included in the statement of financial position in the line item "Tax liabilities".

Special financial activities tax

Special financial activities tax is calculated as 6% of taxable profit exceeding ISK 1,000 million. Special financial activities tax is included in the statement of financial position in the line item "Tax liabilities".

Current tax

Current tax is the expected tax payable on the taxable income for the year using tax rates enacted at the reporting date. Current tax also includes any adjustment to tax payable in respect of previous years. Current tax assets and current tax liabilities are offset in the statement of financial position if the Group has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously. Current tax is included in the statement of financial position in the line item "Tax liabilities".

Deferred tax

Deferred tax is recognised based on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts. However, deferred taxes are not recognised if it arises from the initial recognition of an asset or liability, in a transaction other than a business combination, that at the time of the transaction affects neither the taxable profit nor the accounting profit. In addition, deferred taxes are not recognised if the temporary difference arises from the initial recognition of goodwill.

Deferred tax is measured using tax rates enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. The deferred tax asset is reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax liabilities are included in the statement of financial position in the line item "Tax liabilities" and deferred tax assets are included in the statement of financial position in the line item "Other assets". Deferred taxes that are part of discontinued operations (see Note 67.11) are included in the line items "Non-current assets and disposal groups held for sale" and "Other liabilities", respectively, in the statement of financial position.

67.21 Discontinued operations, net of income tax

Discontinued operations, net of income tax, are disclosed as a separate line item in the income statement and consist of (i) profit or loss from foreclosed assets and disposal groups held for sale, (ii) gain or loss recognised on the measurement to fair value less costs to sell in excess of book value of foreclosed assets, (iii) profit or loss from sales of foreclosed assets and disposal groups held for sale, and (iv) income tax expense from discontinued operations.

67.22 Offsetting

Financial assets and financial liabilities are set off and the net amount reported in the statement of financial position when, and only when, the Group has a legal right to offset the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Group presents income and expenses on a net basis in the income statement only when required or permitted by the accounting standards.

67.23 Earnings per share

The Group presents basic and diluted earnings per share for its ordinary shares. Basic earnings per share are calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period. Diluted earnings per share are determined by adjusting the profit or loss attributable to ordinary shareholders of the Bank and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, if any.

Íslandsbanki's Corporate Governance Statement 2020

Unaudited

Unaudited Appendix: Corporate Governance Statement 2020

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 of the Central Bank (FSA CB) as well as other applicable law and regulations, including those imposed by the FSA CB and Nasdaq Iceland, available at their respective websites (www.cb.is and 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).

Exemplary in Corporate Governance

Íslandsbanki is committed to maintaining high standards of governance complying with best governance practices. Íslandsbanki was first recognised as "Exemplary in Corporate Governance" in March 2014. The recognition was awarded following a comprehensive review of the practices of the Board, Board subcommittees and management. The recognition has been renewed annually since. The recognition is now granted by Stjórnvisi.

Íslandsbanki maintains a Matrix for material bank actions, 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 Matrix for material bank actions sets specific conditions to all major decision-making and requires that all such decisions be 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

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), in accordance with Paragraph 7 of Article 54 of the Act on Financial Undertakings no. 161/2002. The Guidelines are available on www.corporategovernance.is. Governance practices of the Bank are consistent with the Guidelines. Íslandsbanki is in full compliance with them except for Article 1.5.

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 while the Icelandic Government is the sole owner of the Bank. Board members are nominated by the Icelandic State Financial Investments (ISFI) through a selection process administered by the ISFI in accordance with article 7 of Act no. 88/2009 on the Icelandic State Financial Investments.

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 Group 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 approves the risk policy, risk appetite statement and procedure for risk management and ensures that internal procedures for risk management are revised at least annually.

The All Risk Committee, a Senior Management Committee, is comprised of the CEO, all the managing directors of the Bank and other members of management appointed by the CEO. The committee is responsible for the review and implementation of the risk management and internal control policies issued by the Board and monitors that the risk profile of the Bank is within the limits of the risk appetite statement of the Board of Directors. The ARC issues guidelines for risk assessment and individual risk thresholds or limits in accordance with Board approved risk appetite.

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

Unaudited Appendix: Corporate Governance Statement 2020

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 and the Board Audit Committee assists the Board in fulfilling its oversight responsibilities concerning the financial reporting process, the system of internal control and the audit process.

The Bank's Finance division is responsible for the preparation of the Group's consolidated financial statements in line with the International Financial Reporting Standards (IFRS) as adopted by the European Union and additional requirements in the Act on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions. 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 the half year consolidated financial statements and audit the consolidated financial statements.

The consolidated financial statements are published on an annual and quarterly basis.

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. At the 2016 AGM the Icelandic National Audit Office (INAO) was elected, for the first time, to serve as Íslandsbanki's independent external auditing firm, in accordance with Article 4 of Act no. 46/2016 on the Auditor General and the auditing of government accounts for a term of five years. 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

The Chief Audit Executive is appointed by the Board, reports directly to the Board and directs Group Internal Audit with a mandate from the Board. 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 the Board with independent and 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. The responsibilities and authorisations of the CAE and Group Internal Audit are further outlined in the Group Internal Audit Charter.

Compliance

The Bank's Compliance Officer is hired 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 the Bank's responsible officer under the US Foreign Account Tax Compliance Act (FATCA) and the OECD Common Reporting Standard (CRS).

Íslandsbanki Values, Code of Conduct and Sustainability

In 2019 the Bank's strategy was revised and the employees of the Bank played a key role in its formulation. Our purpose is moving Iceland forward by empowering our customers to succeed. Íslandsbanki's values are the pillars of the Bank's corporate culture, shaping the conduct and attitudes of its employees. The values of Íslandsbanki are passion, professionalism and collaboration.

In October 2019 the Board approved a Code of Conduct for the Bank's employees. The aim of the code is to promote good operational practices. The document is available on the Bank's website.

Íslandsbanki seeks to work in harmony with the communities in which it operates and strives to have a positive impact in society. This participation in community programmes rests on Íslandsbanki's Sustainability Policy which is set by the Board. The strategy covers five key areas: business, education, environment, workplace, and community. In addition, the Bank has decided to focus particularly on four of the UN Sustainable Development goals in its course of business: quality education; gender equality; industry innovation and infrastructure; and climate action. Annually the bank publishes an Annual and Sustainability Report in accordance with the Nasdaq ESG guidelines, the applicable Global Reporting Initiative (GRI) metrics, the UN Global Compact, and the SDGs. 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.

The Bank has approved a sustainability policy which is focused on making its operations exemplary in the Iceland business environment based on established international ESG criteria. The Bank aspires to be a leader in sustainable development and to move Iceland forward by empowering its customers to succeed.

Board of Directors

The Board of Directors comprises seven non-executive directors, and one alternate member, 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 hired by the Board.

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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 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 20 times in 2020, each time constituting a quorum.

Candidates for board membership are nominated through a selection process administered by ISFI in accordance with Article 7 of Act no. 88/2009 on Icelandic State Financial Investment. 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. The Board has approved a policy on the suitability of the Board of Directors, the CEO and key function holders. The policy states, among other things, that the composition of the Board shall at any time be diverse, with regard to educational and professional background, gender and age.

The Board subcommittees

The Board subcommittees are three in total and they operate under the terms of a mandate letter from the Board as well as the Rules of Procedure of the Board. The mandate letters of the Board subcommittees are available on the Bank's website. The Board appoints the members of the subcommittees as well as their Chairman. When appointing the subcommittees, the Board shall take into account the expertise, skills and experience needed of a member to be appointed to the relevant subcommittee. All of the subcommittees are constituted of members of the Board.

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 six times in 2020, each time constituting a quorum.

The Board Risk Management Committee, comprising three Board members, assists the Board in providing oversight of senior management 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's responsibilities include the parent company, its subsidiaries and the whole Group. The committee met nine times in 2020, each time constituting a quorum.

The Board Corporate Governance 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 seven times in 2020, each time constituting a quorum.

Structure and composition of Board subcommittees is as follows:

	Board Corporate Governance and HR Committee	Board Audit Committee	Board Risk Management Committee
Hallgrímur Snorrason		Member	Member
Anna Þórðardóttir		Chair	
Árni Stefánsson			Chair
Frosti Ólafsson	Member	Member	
Guðrún Þorgeirsdóttir			Member
Heiðrún Emilía Jónsdóttir	Chair		
Herdís Gunnarsdóttir	Member		

Chair Member

Members of the Board

Hallgrímur Snorrason, Chairman of the Board, (b. 1947) has been Chairman since March 2020 but first joined the Board in April 2016. He is an independent consultant in official statistics at international level. He was Director-General 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 hf., Skýrr and Auður Capital. He has also chaired or served on a number of governmental committees, both domestically and in connection with Nordic cooperation, EFTA, EU and the OECD.

Hallgrímur holds a M.Sc. in Economics from the University of Lund in Sweden and a B.Sc. in Economics from the University of Edinburgh, UK.

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

Anna Þórðardóttir (b. 1960) joined the Board in April 2016. She has been a board member of a number of companies and organisations, 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 is chairman of the Board Audit Committee of Hagar. Anna was an employee of KPMG in 1988-2015, where she became partner in 1999. While at KPMG, she was responsible for the audit of the following companies: Reitir, Hagar, 365, Baugur Group, Vodafone, Landfestar, Landey, 10-11 and Félagsbústaðir.

Anna holds a Cand.oecon. in Business Administration from the University of Iceland and is a Chartered Accountant. She has also studied towards a Cand.merc in Financial studies from Handelhøjskolen in Aarhus, Denmark.

Sub-Committees: Chairman of the Board Audit Committee.

Árni Stefánsson (b. 1966) joined the Board in April 2016. He has extensive management experience in power-intensive industry in Iceland and is currently manager and member of the executive board at the Rio Tinto primary aluminium plant. Previously, he was a manager of the Century Aluminium plant Norðurál in Grundartangi; manager and in the executive board with Landsnet, the electric transmission grid company of Iceland; and manager with Landsvirkjun, the National Power Company of Iceland.

Árni holds an M.Sc. in Electrical Engineering.

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

Frosti Ólafsson (b. 1982) joined the Board in March 2020. He is an independent strategic consultant. He is the former CEO of ORF Genetics, a leading plant biotechnology company that owns and operates the BIOEFFECT skin care brand, and the former Managing Director of Iceland Chamber of Commerce and worked as a strategic consultant for McKinsey & Company. In his past roles, he has supported leading domestic and international companies on a wide range of topics, including strategy, operations and governance. Frosti is currently a Board member at Reykjavik University and affiliated real estate entities, at Freyja Private Equity Fund and a Board member at Controlant.

Frosti holds an MBA degree from London Business School and a B.Sc. degree in economics from University of Iceland and Macquire University in Sydney.

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

Guðrún Þorgeirsdóttir (b. 1979) joined the Board in March 2020. She is the Chief Business Development Officer of PayAnalytics. Previously, Guðrún was the Chief Financial Officer of Skeljungur. Guðrún has prior experience as a Chief Risk Officer and as an investment manager. She is an experienced board member and has served on the board of directors of insurance companies, financial companies and retail and service companies, including VÍS, Lífís, Lyfja and Lýsing.

Guðrún holds an MBA from HEC School of Management in France, has a B.Sc. in Industrial Engineering from the University of Iceland, and is a securities broker licensed by the Icelandic Ministry of Finance and Economic Affairs.

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

Heiðrún Jónsdóttir (b. 1969) joined the Board in April 2016. She is an attorney at law with Múli Legal Services and serves as a member of the board of Reginn, real estate company and Royal Arctic Line. Previously, she was Managing Director at Eimskipafélag Íslands, Lex Legal Services, and Legal and Human Resources at KEA. She has been chairman of the board at Norðlenska, Íslensk Verðbréf and Gildi pension fund and has been a member of the board of Síminn, Icelandair Group, Olíuverzlun Íslands, the Icelandic Banks' Data Centre (RB), Ístak, the securities depository Arion Verðbréfavarsla, Þekking, the Icelandic Pension Funds Association. Heiðrún served as a board member of the board of the Icelandic Bar Association from 2016 -2019 and was the deputy chairman of the board from 2018-2019.

Heiðrún holds a Cand. Jur from the University of Iceland and is a securities broker licensed by the Icelandic Ministry of Finance and Economic Affairs. She completed an Advanced Management Program (AMP) at IESE Business School in Barcelona in 2017.

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

Herdís Gunnarsdóttir (b.1968) joined the Board in November 2020. Herdís is the director of the Icelandic Social Insurance Administration's rights division. She has previously worked, e.g. as the CEO of the Health Care Institute of the South of Iceland. Herdís has extensive experience as a manager in the health sector and in public institutions but has also worked on independent projects in the field of policymaking and project management. In addition to her work, she has taught at universities. Herdís also has extensive experience of serving as a board member in the field of non-governmental organisations, trade- and professional unions and pension funds and in European partnership, of which she was a chairman of a pension fund, and in European Associations.

Herdís holds an MBA from the University of Iceland, an M.Sc. degree in paediatric nursing and a B.Sc. degree in nursing, from the University of Iceland.

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

Flóki Halldórsson (b. 1973) served on the Board from March 2020 until November 2020. Flóki resigned from the Board when he was appointed head of the office of the Resolution Authority of the Central Bank of Iceland. Herdís Gunnarsdóttir, who had been an alternate member of the Board since April 2016, replaced Flóki.

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The alternate member of the Board is Óskar Jósefsson, since March 2020.

None of the members of the Board owns shares in the Bank, neither as a direct ownership nor through associated parties. All members of the Board are as well considered independent from the Bank, its main clients, competitors and shareholder.

Board Performance and Suitability 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 an assessment of the necessary number of board directors, the board structure in relation to knowledge and experience, board procedure and practices. This assessment was last performed by the Board in December 2020.

Furthermore, the Board annually assesses the collective suitability of the Board and individual Board members in accordance with the Board's Rules of Procedure and the Bank's policy on the assessment of the suitability of the Board of Directors, the CEO and key function holders.

The Chief Executive Officer

The Chief Executive Officer (CEO) is responsible for the day-to-day operations of the Bank and that the Bank's business is, at all times, in accordance with the Bank's Articles of Association, policies of the Board and the relevant law. The CEO engages the Bank's Compliance Officer and appoints members of the Executive Committee and other Senior Management Committees.

Birna Einarsdóttir (b. 1961) is the CEO of Íslandsbanki. She holds an MBA from the University of Edinburgh, UK and a Cand.oecon. in Business Administration from the University of Iceland. Birna first started working with Íslandsbanki's predecessors in 1987 and has been 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 considered independent from the Bank, its main clients, competitors and shareholder.

The CEO is not a shareholder in the Bank, neither directly nor indirectly. No call-option agreements exist between the CEO and the Bank.

The executive committee

The executive committee consists of seven people, including the CEO: Birna Einarsdóttir, CEO since October 2008, Jón Guðni Ómarsson, Chief Financial Officer since October 2011, Sigríður Hrefna Hrafnkelsdóttir, Managing Director of Personal Banking since May 2017, Riaan Dreyer, Director of Information Technology since September 2019, Guðmundur Kristinn Birgisson, Chief Risk Officer since October 2018, Una Steinsdóttir, Managing Director of Business Banking since May 2017 and, Ásmundur Tryggvason Managing Director of Corporate & Investment Banking since January 2019.

Senior Management Committees

Senior Management Committees are advisory committees appointed by the CEO. Senior Management Committees are divided into Executive Committees and Business Committees. The committees are appointed by the CEO, and their letters of mandate and rules of procedure are documented in a charter set by the CEO.

The Executive Committee and the All Risk Committee are responsible for the implementation of the Board approved business strategy, risk appetite and policies and consist of the CEO, all managing directors as well as other members of senior management appointed by the CEO.

- The Executive Committee, chaired by the CEO, is responsible for implementing the Board approved business strategy.
- The All Risk Committee is responsible for the review and implementation of the risk management and internal control policies issued by the Board and monitors that the risk profile of the Bank is within the limits of the risk appetite statement of the Board of Directors.

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The Business Committees decide on individual business proposals in accordance with the rules and procedures issued by the All Risk Committee, the Executive Committee and the Board. The Bank's Business Committees are the Asset and Liability Committee, the Senior Credit Committee, the Investment Committee, the Operational and Security Committee and the Sustainability Committee.

- The Senior Credit Committee decides on proposals on lending and is the formal venue for discussion and review of individual loan proposals.
- The Asset and Liability Committee decides on proposals regarding market risk, liquidity risk, funding, capital and internal and external pricing.
- The Investment Committee decides on proposals regarding the purchase, sale and valuation of equity stakes and other investments of the Bank.
- The Operational and Security Committee decides on proposals regarding new products and services, continuous operation and material changes in systems and procedures.
- The Sustainability Committee is a formal forum for reviewing and discussing issues related to sustainability risk, sustainable procurement and business opportunities.

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 applicable law, rules, regulations and guidelines.

The Bank is wholly owned by the Icelandic Government since January 2016. The shares are administered by Icelandic State Financial Investments (ISFI) in accordance with the Act on Icelandic State Financial Investments no. 88/2009. Shareholders' meetings, the supreme authority of the Bank, are the general forum for informing and communicating with shareholders. Following each publishing of financial results of the Bank a meeting is held with the ISFI to present the relevant financial results. 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.

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

In the year 2020 no remarks were received from an appropriate supervisory or ruling body concerning violations of laws or regulations. Information on legal cases relating to Íslandsbanki can be found in the notes to the consolidated financial statements.

This Corporate Governance Statement was approved by Íslandsbanki's Board of Directors on 10 February 2021.