

Economic and monetary chronicle 2009

January

On January 1, the Iceland Civil Aviation Administration operations at Keflavík Airport and Leifur Eiríksson International Airport were merged into a State-owned corporation called Keflavik Airport Ltd.

On January 2, the listing of the exchange rate index was discontinued. The old index, which bore the abbreviation GVT, was replaced with an index based on a narrow trade basket (TWI), which was recalculated so that its January 2 value equalled that of the GVT index.

On January 6, the Government announced that it would thoroughly investigate the possibility of seeking legal remedy before the European Human Rights Court because of the UK authorities' application of the Anti-Terrorism, Crime and Security Act of 2001 against Landsbanki in late 2008. The Government also reiterated that it would support legal action by the Kaupthing resolution committee because of the British Financial Services Authority's conduct against Kaupthing subsidiary Singer & Friedlander on October 8, 2008. It will also support possible legal action taken by the Landsbanki resolution committee against the British authorities.

On January 8, Fitch Ratings announced that it had affirmed its ratings for Kaupthing Bank hf., Landsbanki Íslands hf., and Glitnir hf. (the old Icelandic banks). The ratings for short- and long-term obligations were affirmed at D, the support rating was 5, and the individual rating was F. The agency also announced that it would no longer assign credit ratings for the banks.

On January 23, Moody's Investors Service released its annual sovereign credit report on the Republic of Iceland. The report stated that Moody's still considered Iceland an investment-grade country despite the current financial and economic crisis and the challenges it faces. However, the negative outlook for the Baa1 rating was maintained because "the economic outlook remains uncertain and could quickly change."

On January 26, the coalition government between the Independence Party and the Social Democratic Alliance was dissolved. A coalition between the Social Democratic Alliance and the Leftist Green Party assumed control on February 1, under the leadership of Prime Minister Jóhanna Sigurðardóttir.

On January 28, the Ministry of Finance published a statement of Treasury assets and liabilities. It is assumed that the Treasury's total liabilities will rise by just over 400 b.kr. in 2009. In addition, the Treasury will guarantee the debt due to Icesave/Edge and the loans from the IMF and others to the Central Bank of Iceland, in the amount of almost 1,300 b.kr. The Treasury's debt is estimated to approach 1,100 b.kr. by year-end 2009. According to the National Budget for 2009, the Treasury deficit for the year will be 150 b.kr.

On January 29, the Board of Governors of the Central Bank of Iceland decided to hold the Bank's policy interest rate unchanged at 18%.

February

On February 3, the Minister of Health cancelled the consultation fee charged by hospitals and health care institutions. The previous regulation, set on December 29, 2008, was revoked.

On February 9, Moody's Investors Service announced that it had lowered (old) Kaupthing Bank hf.'s credit rating for long-term obligations from Caa1 to C. The bank's short-term obligations are still rated as "Not Prime" and the financial strength rating is E.

On February 11, Moody's Investors Service announced that it had lowered (old) Glitnir Bank hf.'s credit rating for long-term obligations from Caa1 to C. The bank's short-term obligations are still rated as "Not Prime" and the financial strength rating is E.

On February 12, the International Monetary Fund published a report entitled, "Iceland-SBA-Review Under the Emergency Financing Mechanism", about the progress of the economic programme drafted by the Fund and the Government of Iceland. The report was a part of the Stand-By Arrangement granted by the IMF to the Icelandic Government on November 19, 2008, and was written following the visit to Iceland by the IMF mission on December 15-19, 2008.

On February 19, the District Court of Reykjavík extended Kaupthing and Glitnir's moratoria on payment until November 13, 2009.

On February 25, the Icelandic Federation of Labour (ASÍ) and the Confederation of Icelandic Employers (SA) agreed to postpone the implementation of the negotiated wage increases that were to take effect on March 1, and to postpone their review of contractual wage settlements for up to four months. Despite the postponement of general wage hikes, the agreement contained a provision stipulating that minimum wages should rise to 157,000 kr. and that several other provisions should take effect, including lengthened vacation time.

On February 26, Parliament passed legislation amending the Act on the Central Bank of Iceland. The new Act provides for one Governor and one Deputy Governor within the Central Bank instead of a Board of Governors. The Governor and Deputy Governor are to be appointed following advertisement of the positions; applicants must have completed a master's degree in economics or a related field and must possess extensive experience and knowledge of monetary issues. Decisions on the application of the Bank's monetary policy instruments will henceforth be made by a Monetary Policy Committee, but in other respects, the Bank's direction shall be in the hands of the Governor. In this context, the Bank's monetary policy instruments include decisions on interest rates, specified transactions with credit institutions, determination of reserve requirements, and currency market transactions intended to influence the exchange rate of the króna. Upon the entry into force of the amendment, the Board of Governors was abolished, as were the positions of the three governors then constituting the Board.

On February 27, the Prime Minister appointed Svein Harald Øygard and Arnór Sighvatsson to temporary positions as Central Bank Governor and Deputy Governor, respectively, in accordance with the amended Central Bank Act. They will remain in office until the Prime Minister has made permanent appointments on the basis of an advertisement pursuant to the provisions of the Act.

March

On March 3, the District Court of Reykjavík extended Landsbanki Íslands hf.'s moratorium on payment until November 26, 2009.

On March 3, the Governor of the Central Bank decided that Thórarinn G. Pétursson, Acting Chief Economist of the Central Bank, should take a seat on the Monetary Policy Committee. Other members include Central Bank Governor Svein Harald Øygard, who also chairs the Committee, and Deputy Governor Arnór Sighvatsson. That same day, the Prime Minister appointed two external representatives, Dr. Gylfi Zoëga and Dr. Anne Sibert, to the Monetary Policy Committee.

On March 5, Parliament agreed to repeal an act of law from 2003 concerning retirement income for the president of Iceland, governmental ministers, members of Parliament, and Supreme Court judges. Their terms of remuneration in retirement will henceforth be on a par with those of other civil servants.

On March 6, Parliament passed legislation providing for 100% reimbursement of value-added tax on on-site labour for construction work done on residential property. The increased reimbursement percentage applies to the period March 1, 2009 to July 1, 2010.

On March 9, the Financial Supervisory Authority announced that it had intervened in the operations of Straumur-Burdaras Investment Bank hf. on the basis of the provisions of Article 100(a) of the Act on Financial Undertakings, no. 161/2002. The Financial Supervisory Authority appointed a resolution committee, which assumed all of the authorisations of Straumur's Board of Directors.

On March 9, Fitch Ratings announced that it had lowered Straumur- Burdaras Investment Bank's rating for long-term obligations from B to D. The agency has stopped issuing ratings for Straumur.

On March 10, Moody's Investors Service announced that it had lowered (old) Landsbanki Íslands hf.'s credit rating for long-term obligations from Caa1 to C. The bank's short-term obligations are still rated as "Not Prime" and the financial strength rating is E. Moody's also announced that it had stopped issuing ratings for the bank.

On March 10, Parliament authorised owners of private pension savings to withdraw up to 1 m.kr. over a nine-month period. The authorisation covers applications submitted between March 1, 2009, and October 1, 2010.

On March 13, the International Monetary Fund mission completed a fifteen-day visit to Iceland. The visit, whose purpose was to review the economic programme prepared by the Fund and the Icelandic Government, was conducted in connection with the USD 2.1 billion Stand- By Arrangement approved for Iceland by the Executive Board of the Fund on November 19. The mission met with Government officials, members of Parliament, and representatives of the private sector and labour organisations.

On March 17, Parliament passed an amendment to the Act on Securities Transactions. The amendment reduced the threshold for mandatory takeover bids from 40% to 33% but provided for exemptions under which, in certain instances, a holding may exceed the threshold without creating a takeover requirement.

On March 17, Parliament passed a statutory amendment authorising the Financial Supervisory Authority to publish the results of its investigations except in exceptional circumstances.

On March 19, the Monetary Policy Committee of the Central Bank of Iceland decided to lower the Bank's policy interest rate by 1.0 percentage point, to 17%.

On March 19, the District Court of Reykjavík granted Straumur-Burdaras Investment Bank hf. a moratorium on payment.

On March 21, the Financial Supervisory Authority announced that it had intervened in the operations of Reykjavík Savings Bank hf (SPRON) on the basis of the provisions of Article 100(a) of the Act on Financial Undertakings, no. 161/2002. The Financial Supervisory Authority appointed a resolution committee, which assumed all of the authorisations of SPRON's Board of Directors.

On March 21, the Financial Supervisory Authority announced that it had intervened in the operations of Sparisjóðabanki Íslands hf. on the basis of the provisions of Article 100(a) of the Act on Financial Undertakings, no. 161/2002.

On March 23, the District Court of Reykjavík granted Sparisjóðabanki Íslands hf. a moratorium on payment.

On March 26, a Government loan facility was announced. The facility was arranged with VBS Investment Bank and Saga Capital because of the debts that the Treasury took over from the Central Bank. The banks will receive indexed seven-year loans at 2% interest. The loan is subject to various security-related terms and conditions.

On March 27, the Financial Supervisory Authority announced that it appointed a resolution committee for Sparisjóðabanki Íslands hf. on the basis of the provisions of Article 100(a) of the Act on Financial Undertakings, no. 161/2002. The resolution committee assumed all of the authorisations previously held by the bank's Board of Directors.

On March 30, the report prepared by Finnish banking expert Kaarlo Jännäri was made public. The report centred on the regulatory framework and supervision of banking operations and contained various comments and suggestions for improvements. The Government then appointed a work group to examine the recommendations in the report.

On March 30, Parliament approved amendments to the Act on Bankruptcy, etc., which centre on payment mitigation measures designed to support individuals in severe financial distress. According to the amended Act, an individual may seek composition of creditors for the purpose of payment mitigation if he can demonstrate that he

cannot fulfil his financial commitments and will be unable to do so for the foreseeable future. Under debt mitigation, it is possible to stipulate full cancellation of contractual claims; proportional reduction of such claims; deferral of payment; payment with a share in the instalment amount, either in a single payment or at given intervals during a further specified period of time; change in the form of payment; or the last four of these simultaneously.

On March 30, Parliament passed legislation on guarantors, which includes provisions on required disclosure of information to prospective guarantors and exempts a guarantor's real property from settlement if a claim should fall on him.

On March 31, Parliament agreed to tighten foreign exchange restrictions with amendments to the Customs Act and the Foreign Exchange Act. A new temporary provision added to the Foreign Exchange Act stipulates that exports of goods and services shall take place in foreign currency. The amendment to the Customs Act requires that the transaction price on exportation reports be listed in foreign currency and that it be based on the currency appearing on the exporter's sales invoice, but not Icelandic krónur.

April

On April 3, the Financial Supervisory Authority announced that it had intervened in the operations of SPM Savings Bank, at the savings bank's request, on the basis of the authority contained in Article 00(a) of the Act on Financial Undertakings, no. 161/2002. The savings bank's assets and liabilities were allocated in accordance with a purchase agreement with New Kaupthing hf. and an agreement with the savings bank's largest creditors.

On April 8, the Monetary Policy Committee of the Central Bank decided to lower the collateral loan rate by 1.5 percentage points to 15.5%. Other Central Bank interest rates were also lowered by the same amount.

On April 8, an agreement was announced between the Ministry of Business Affairs and credit institutions that grant foreign-denominated loans, extending the payment smoothing option for indexed loans to cover foreign-denominated loans as well.

On April 15, Parliament passed Act no. 46/2009 amending the Income Tax Act. The main provisions of the amendment are as follows:

i) parties with interest income in Iceland shall be required to pay tax on that income; ii) cancelled debt in accordance with composition of creditors agreements providing for debt mitigation is not considered income; iii) provisions are to be adopted for the taxation of residents that own companies domiciled in low-tax countries.

On April 15, Parliament passed Act no. 44/2009, which amends the provisions in the Act on Financial Undertakings pertaining to the delivery of a financial undertaking to an interim Board of Directors and the requirements for and commencement of winding-up proceedings.

On April 15, Parliament passed Act no. 45/2009, which provides for increases in household mortgage interest allowances. The increase in 2009 was estimated to total 2 b.kr.

On April 15, Parliament passed Act no. 50/2009 on temporary payment mitigation of residential mortgage loans, which can be offered to debtors for up to five years.

On April 17, Parliament passed Act no. 51/2009, which authorises the Minister of Industry to negotiate with prospective owners concerning the construction of an aluminium smelter at Helguvík. Among other provisions, the Act stipulates that the activities of the smelter shall be exempt from future amendments to the principal provisions of the Income Tax Act that may be onerous.

On April 18, agreements between the Minister of Agriculture and the Farmers' Association of Iceland were announced. The agreements set forth provisions for agricultural subsidies over the next few years. According to the agreements, payments will rise by 2% in both 2010 and 2011, and they will also rise by half of the accumulated non-fulfilment of the original agreements, up to a maximum total amount of 5%. In 2012, payments will rise to the amount specified in current agricultural subsidy agreements, subject to a maximum of 5%.

On April 22, the Financial Supervisory Authority announced that Deloitte LLP had completed its valuation of the assets transferred from the old banks in order to form the balance sheets of New Kaupthing Bank, NBI, and Íslandsbanki. Concurrent with this, the consulting firm Oliver Wyman completed its appraisal of the valuation.

On April 24, the Competition Authority announced that commercial banks, savings banks, pension funds, and the Housing Financing Fund were authorised to take co-ordinated action to assist individual mortgage holders in financial distress. Without such authorisation, concerted action of this type could have been in violation of the Competition Act.

On April 27, the District Court of West Iceland granted SPM Savings bank a moratorium on payment.

May

On May 7, the Monetary Policy Committee of the Central Bank decided to lower the collateral loan rate by 2.5 percentage points to 13.0%. Overnight lending rates were also lowered by 2.5 percentage points, and other Central Bank rates were reduced by 3 percentage points.

On May 10, the coalition government of the Social Democratic Alliance and the Left-Green Movement assumed power.

On May 12, the District Court of Reykjavík appointed a winding-up committee for Straumur-Burðarás Investment Bank hf.

On May 22, the District Court of Reykjavík appointed a winding-up committee for Sparisjóðabanki Íslands hf.

On May 28, Parliament passed Act no. 60/2009, raising alcoholic beverage and tobacco taxes, oil charges, and motor vehicle taxes, while lowering per-kilometre charges. The change was intended to generate some 4.4 b.kr. annually for the Treasury.

June

On June 4, the Monetary Policy Committee of the Central Bank decided to lower the collateral loan rate by 1 percentage point to 12.0%. The overnight lending rate was also lowered by 1 percentage point.

On June 5, agreements between the governments of Iceland and the Netherlands, on the one hand, and Iceland and the United Kingdom, on the other, were signed. The agreements provide for the liability of the Icelandic Depositors' and Investors' Guarantee Fund for deposits in Landsbanki branches in the two countries, as well as for a Government guarantee of the Fund's financing. The agreements were signed by Iceland subject to parliamentary approval of the Government guarantee.

On June 24, the District Court of Reykjavík approved a request to appoint winding-up committees for SPRON hf. and Frjálsi Investment Bank hf.

On June 26, the Prime Minister appointed Már Guðmundsson as Governor of the Central Bank, effective August 20, and Arnór Sighvatsson as Deputy Governor, effective July 1.

On June 29, Parliament passed Act no. 70/2009, which sets forth various fiscal measures. The measures include the following:

- i) raising the payroll tax by 1.56% of the tax base and raising the contribution to the Wage Guarantee Fund by 0.1% of wages;
- ii) levying a separate 8% tax on individual income in excess of 700,000 kr. per month, irrespective of the spouse's income;
- iii) raising the tax on financial income from 10% to 15% on such income in excess of 42,000 kr. per month and accelerating the collection of the tax,
- iv) tightening income-linking and reducing the tax-free threshold in the social security system,
- v) reducing childbirth leave benefits,

- vi) limiting Government payments to victims and restricting entitlement to indigent party status,
- vii) revoking payments to the University of Iceland in the amount of parish fees for persons outside organised religious groups.

Estimated revenues from tax code amendments amounted to 17 b.kr. on a full-year basis, and 8.6 b.kr. in 2009, excluding the Treasury's payroll tax payments to itself. The reduction in expenditure was estimated at 4.5 b.kr. on a full-year basis, and 2.2 b.kr. in 2009.

July

On July 1, an agreement was signed between Iceland, on the one hand, and Norway, Denmark, Finland, and Sweden, on the other, concerning a loan of 1775 million euros from the four Nordic countries to Iceland.

On July 1, revised Rules on Central Bank of Iceland Facilities for Financial Undertakings, no. 553 of June 26, 2009, took effect. The new Rules provided for two major changes. On the one hand, eligibility rules concerning collateral for Central Bank facilities were tightened. The main securities eligible as collateral for Central Bank of Iceland facilities are now Housing Financing Fund bonds, Treasury notes, and Treasury bills. The new Rules also contain provisions that expand and clarify the Central Bank's authorisation to manage market liquidity.

On July 2, the Monetary Policy Committee decided to hold the collateral loan rate unchanged at 12.0%.

On July 3, the Financial Supervisory Authority appointed a threemember interim Board of Directors for SPM Savings Bank on the basis of Article 100(a) of the Act on Financial Undertakings, no. 161/2002, as amended by Act no. 44/2009.

On July 10, the Minister of Fisheries announced the decision on fishing quotas for the principal non-pelagic species in the 2009-2010 fishing year. The quota permitted catches amounting to 150,000 tonnes of cod, 50,000 tonnes of perch, 63,000 of haddock, and 50,000 tonnes of pollock. The total allowable catch for haddock was reduced by 30,000 tonnes between years, and the cod quota by 12,500 tonnes.

On July 10, Parliament passed Act no. 75/2009, which provides for the establishment of a State-owned limited liability company to support the restructuring of viable non-financial firms.

On July 10, Parliament passed Act no. 73/2009, amending the Foreign Exchange Act. The amendments expand the Financial Supervisory Authority's investigative authority and include penalty provisions for unauthorised intermediation in foreign exchange transactions.

On July 10, Parliament passed Act no. 76/2009, amending the Act on Financial Undertakings. The new amendment makes extensive changes in the legal environment of savings banks. It clarifies provisions on their operational form, revokes their authorisation to convert to limited liability companies, simplifies and tightens the rules on dividend payments, and adds rules on changes to guarantee capital.

On July 16, Parliament authorised the Government to apply for European Union membership. That same day, the Prime Minister, on behalf of the Government, sent the European Union an application for membership for Iceland.

On July 20, the Ministry of Finance announced that agreements had been reached with the resolution committees of the three commercial banks – Glitnir, Kaupthing, and Landsbanki – concerning capitalisation and settlement of assets. The agreement entailed offering the resolution committees of Glitnir and Kaupthing the possibility of acquiring a majority holding in Íslandsbanki and New Kaupthing. In the case of Landsbanki, the agreement centred on the arrangements for continuing negotiations. All of the agreements were subject to the final decision of the resolution committees, which was to be taken following consultation with creditors. They were also subject to the approval of the Financial Supervisory Authority, which must determine whether the actions taken are in compliance with funding requirements, the banks' strength, and the position of the owners at any given time.

August

On August 5, the Central Bank announced its strategy for the phased removal of the capital controls. The first phase entails the liberalisation of capital inflows and investment. The liberalisation strategy ensures that assets thus flowing into the country can be expatriated again, provided that they are registered with the Central Bank. In later phases, restrictions on capital outflows will be lifted, first on long-term obligations and then on short-term assets.

On August 11, Parliament elected a new Central Bank Supervisory Board following a proportional election, in accordance with Article 26 of the Act on the Central Bank of Iceland, no. 36 of May 22, 2001. Elected Board members are Lára V. Júlíusdóttir, Ragnar Arnalds, Ágúst Einarsson, Hildur Traustadóttir, Ragnar Árnason, Magnús Árni Skúlason, and Katrín Olga Jóhannesdóttir. The following were elected as alternates: Margrét Kristmannsdóttir, Anna Ólafsdóttir Björnsson, Björn Herbert Guðbjörnsson, Guðrún Ágústa Guðmundsdóttir, Birgir Þór Runólfsson, Ingibjörg Ingadóttir, and Friðrik Már Baldursson. At the first meeting of the new Supervisory Board, Lára Júlíusdóttir was elected Chairman and Ragnar Arnalds was elected Vice-Chairman. Daniel Gros was elected to replace Magnús Árni Skúlason on October 15, 2009.

On August 11, Parliament passed the Act on the Iceland State Banking Agency, no. 88/2009, which provides for a Government institution whose role is to administer the State's holdings in financial institutions.

On August 13, the Monetary Policy Committee decided to hold the collateral loan rate unchanged at 12.0%.

On August 14, the Ministry of Finance announced that Government funding for Íslandsbanki and New Kaupthing was assured. The funding was approved at shareholders' meetings and was in line with proposals that had been announced on July 20. The banks' equity was contributed in the form of Treasury bonds and corresponded to a capital adequacy ratio of approximately 12%.

On August 28, Parliament passed Act no. 98/2009, which amends a number of laws due to the transfer of tasks within the Government of Iceland. Among other changes, all tasks related to economic policy, including the administration of Statistics Iceland and the Central Bank of Iceland, were transferred from the Prime Minister's Office and the Ministry of Finance to the Ministry of Economic Affairs. Consumer affairs and property registration were transferred to the Ministry of Justice and Human Rights, and ownership of the State-owned farmsteads and publicly owned companies previously administered elsewhere was transferred to the Ministry of Finance.

On August 28, Parliament passed Act no. 96/2009, authorising the Minister of Finance to guarantee the Depositors' and Investors' Guarantee Fund's obligations for the Landsbanki Icesave accounts in the Netherlands and the UK. The authorisation was subject to a number of reservations, mainly that the so-called Brussels guidelines, from November 14, 2008, on the consideration of Iceland's extraordinary circumstances should apply to the agreements, that State assets should enjoy immunity according to international law, and that annual payments to the UK and the Netherlands should not exceed 4% and 2%, respectively, of accumulated GDP growth since 2008.

September

On September 3, Fitch Ratings published its sovereign credit ratings for the Republic of Iceland. The ratings were unchanged since October 2008: A- for domestic obligations, BBB- for foreign long-term obligations, and F3 for foreign short-term obligations. The outlook remains negative. The domestic rating is higher than the foreign rating because the domestic bond market is considered relatively strong.

On September 4, the Ministry of Finance announced that the Icelandic Government and the Kaupthing resolution committee had signed a settlement agreement pertaining to assets transferred from Kaupthing to New Kaupthing in October 2008. The settlement agreement is in accordance with the agreement announced on July 20, 2009. As was announced on August 14, the Treasury contributed capital to New Kaupthing in the form of Treasury bonds amounting to 72 b.kr., which corresponds to a capital adequacy ratio of approximately 12%. Like the agreement announced on July 20, the agreement authorises the Kaupthing resolution committee, upon consulting with creditors, to acquire an 87% stake in New Kaupthing. This would reduce the Icelandic Government's stake to 13%, and a large portion of its capital contribution would be reversed. If creditors do not exercise this option, the Icelandic

Government will remain the owner of the bank; however, the creditors will retain an option to purchase up to 90% of share capital in the bank between 2011 and 2015, at terms that guarantee the State a suitable return on its investment in the bank.

On September 13, the Ministry of Finance announced that the Icelandic Government and the Glitnir resolution committee had signed a settlement agreement pertaining to assets transferred from Glitnir to Íslandsbanki in October 2008. The settlement agreement is in accordance with the agreement announced on July 20, 2009. As was announced on August 14, the Treasury contributed capital to Íslandsbanki in the form of Treasury bonds amounting to 65 b.kr., which corresponds to a capital adequacy ratio of approximately 12%. The agreement authorises the Glitnir resolution committee, upon consultation with creditors, to acquire 95% of share capital in Íslandsbanki. The Icelandic Government's stake would then be 5%, and a large portion of its capital contribution would be reversed; however, the Government would continue to support the bank with its holding and with a 25 b.kr. subordinated loan. If creditors choose not to exercise this option, the Icelandic Government will remain the owner of the bank. The payment for transferred assets will then be remitted with a bond issued by Íslandsbanki. Furthermore, the creditors will be granted the option of purchasing up to 90% of share capital in the bank between 2011 and 2015, at terms that guarantee the State a suitable return on its investment in the bank.

On September 24, the Monetary Policy Committee decided to keep the collateral loan rate and the interest rate on financial institutions' current accounts unchanged at 12% and 9.5%, respectively. Overnight lending rates were lowered by 1.5 percentage points to 14.5%. The Committee also decided that the Bank should auction 28-day certificates of deposit with a minimum bid rate of 9.5% and a maximum of 10%. The first auction was held on September 30.

October

On 1 October, the District Court of West Iceland authorised SPM Savings Bank to seek composition of creditors agreements.

On 1 October, the Financial Supervisory Authority granted Íslandsbanki hf. and SAT Holding Company hf. permission to own a qualifying holding in SA tryggingar hf. SA tryggingar hf. has two shareholders: Íslandsbanki hf., with 9.3% of share capital, and SAT Holding Company hf., with the equivalent of 90.7% of share capital. SAT Holding Company hf. is wholly owned by Glitnir Bank hf. SA tryggingar took over the insurance operations of Sjóva Almennar on 21 September.

On 4 October, an agreement was signed concerning a loan taken by Treasury in Poland, in the amount of 630 million Polish zlotys, or about 200 million US dollars. The loan term is 12 years, with no instalments paid in the first five years. It will be paid up during the period 2015-22. The interest rate is 2% over and above comparable Polish Government bonds.

On 12 October, the Icelandic government, the Landsbanki Islands hf. resolution committee, and Landsbankinn (NBI hf.) signed an agreement on the settlement of assets and liabilities of the old Landsbanki.

On 15 October, the Ministry of Finance, Íslandsbanki, and the Glitnir resolution committee announced that the resolution committee, on behalf of creditors, had decided to exercise the option set forth in the agreement with the Icelandic Government and acquire a 95% stake in Íslandsbanki.

On 18 October, the round of Icesave negotiations that began after 28 August 2009, when Parliament passed the bill providing a conditional State guarantee for the obligations of the Depositors' and Investors' Guarantee Fund, was concluded.

On 22 October, the Icelandic Government submitted to the European Commission its answers to a 2,600-item questionnaire connected with Iceland's application for EU membership.

On 27 October, the Iceland State Banking Agency (ISBA) assumed ownership of the three commercial banks. Contractual agreements will still be finalised under the auspices of the Minister of Finance. The ISBA operates pur-

suant to Act no. 88/2009. Its role is to administer the State's holdings in financial companies. The ISBA shall have completed its work no later than five years after its establishment.

On 28 October, the Executive Board of the International Monetary Fund (IMF) approved the First Review of Iceland's macroeconomic

programme, thereby authorising the disbursement of the next tranche of the IMF loan to Iceland, in the amount of 167.5 million US dollars (21 b.kr.). Thereafter, the Icelandic Government was able to draw on supplementary credit lines from the Nordic countries, in the amount of 300 million euros. At the request of the Icelandic Government and due to delays in the implementation of the programme, it was also agreed to extend the IMF Stand-by Arrangement by six months, or until 31 May 2011. Disbursements will be adjusted to reflect this change.

On 28 October, the Icelandic Federation of Labour and the Confederation of Icelandic Employers decided not to activate the termination clause in private sector wage agreements. As a result, the wage agreements remain in effect until end-November 2010, with agreed wage changes taking effect on 1 November 2009 and 1 June 2010.

On 31 October, the Minister of Social Affairs signed an agreement with Iceland's major credit institutions, providing for automatic payment smoothing and an extension of indexed mortgage loans by a maximum of three years. An act of law to this effect had been passed by Parliament on 23 October. In addition, it was agreed that these measures would also be available, at the debtor's request, for foreigndenominated mortgages, as well as indexed or foreign-denominated motor vehicle loans that are not in arrears. The reference date was set at January 2008 for indexed loans and 2 May 2008 for foreigndenominated loans. If the loan concerned was taken after these dates, however, the date of the loan shall be the reference date.

On 31 October, the Central Bank of Iceland announced the first phase in the removal of the capital controls. Capital inflows for new investments and subsequent outflows stemming from those investments were authorised. As such, investors are authorised, without restrictions, to convert into foreign currency the sales proceeds from assets in which they invest after 1 November 2009. In addition, a number of technical changes were made to the capital controls in order to reduce circumvention and facilitate implementation.

November

On 5 November, the Central Bank of Iceland Monetary Policy Committee decided to reduce interest rates on deposit institutions' current accounts by 0.5 percentage points, to 9.0%. The maximum amount in weekly auctions of 28-day certificates of deposits was raised from 25 b.kr. to 30 b.kr., with a minimum bid rate of 9.5% and a maximum of 10.25%. This represented a 0.25 percentage point increase in the maximum rate. Interest on seven-day collateral loans was reduced from 12.0% to 11.0%, and overnight lending rates were cut from 14.5% to 13.0%

On 6 November, Parliament passed amendments to the Act on Forced Sale, no. 90/1991, deferring the decision on final sale of residential property until after 28 February 2010, at the debtor's request and upon fulfilment of the requirements set forth in the Act.

On 11 November, Moody's Investors Service lowered the Republic of Iceland's credit ratings for long-term obligations in foreign and domestic currency from Baa1 to Baa3, and for short term obligations from P-2 to P-3. The outlook for all ratings was changed from negative to stable.

December

On 1 December, the Kaupthing resolution committee, upon consultation with creditors and considering the advice of experts, decided that Kaupthing, and therefore the creditors, would acquire 87% of share capital in Arion Bank. The State will retain ownership of 13% of share capital. In capitalising the bank, the State pledged to contribute 72 b.kr. in equity. According to the agreement, the Kaupthing resolution committee will contribute 66 b.kr. instead of the State.

On 4 December, the EFTA Surveillance Authority (ESA) handed down an interim decision on a complaint about the Emergency Act, no. 125/2008, filed by a group of general creditors against the old banks. The interim conclusion

was that the provisions of the Act, particularly those concerning the priority assigned to deposits and the Icelandic Government's actions based on the Act, were in compliance with the EEA Agreement and other legal requirements. The ESA pointed out that no other measures had been available in order to prevent a total collapse of the Icelandic economy.

On 10 December, the Central Bank of Iceland Monetary Policy Committee decided to reduce interest rates on deposit institutions' current accounts by 0.5 percentage points, to 8.5%. The Bank will continue to auction 28-day CDs, although the maximum bid rate will be 9.75% instead of 10.25%. Interest on seven-day collateral loans was reduced from 11.0% to 10.0%, and overnight lending rates were cut from 12.5% to 11.5%.

On 1–4 December, a mission from the International Monetary Fund (IMF) visited Iceland. The mission was led by Mark Flanagan.

On 15 December, the supplementary budget for 2009 was approved by Parliament. Treasury revenues increase by 14.8 b.kr. over and above the National Budget, primarily due to interest income and despite the fact that revenues from the proposed sale of embassy assets are reduced by 5 b.kr. Treasury expenditures rise by 13 b.kr., primarily due to unemployment benefits, mortgage interest allowances, and agricultural subsidies, while expenditures for pension benefits and investment expenses decline.

On 15 December, the Minister of Social Affairs adjusted the guideline amounts for municipal financial assistance upwards by 8.63%, effective 1 January 2010. The change was proportional to the rise in consumer prices, as is stipulated in the agreement between the Ministry and the Association of Local Authorities.

On 16 December, it was announced that the resolution committee and creditors of Landsbanki had decided to acquire 19% of share capital in the new bank, NBI. The Icelandic Government contributes 81% of share capital in Landsbanki, or 122 b.kr. of a total of 150 b.kr. The

new bank will issue a 260 b.kr. foreign-denominated 10-year bond to creditors. This is the minimum valuation of appropriated assets in excess of liabilities. If the recovery is greater, the bank will issue further bonds in exchange for creditors' shares.

On 16 December, Parliament passed Act no. 116/2009, thereby agreeing to act on comments by the EFTA Surveillance Authority (ESA) pertaining to points regarding the implementation of EU Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, via Act no. 64/2006, and concerning, among other things, the reliability of information and the scope of legislation on measures to combat money laundering and terrorist financing.

On 17 December, Parliament agreed, with Act no. 126/2009, to implement EU Directive 2007/36/EC of 11 July 2007, on the exercise of certain rights of shareholders in listed companies, and the Act on Private Limited Companies. The principal amendment is that the minimum advance notice for calling shareholders' meetings in companies that are listed on regulated securities markets has been lengthened from one week to three. Further changes focus, among other things, on increasing the rights and influence of shareholders and ensuring non-discrimination among shareholders, whether domestic or foreign, as regards participation in shareholders' meetings and voting in the companies concerned.

On 18 December, Parliament passed Act no. 120/2009, which entailed changes to various types of social security benefits, particularly with the aim of strengthening the Treasury's operating performance.

On 18 December, Parliament passed Act no. 134/2009, amending legislation on unemployment benefits. The Directorate of Labour's penalties and follow-up measures were strengthened, and the authorisation to pay benefits for curtailed employment percentages was extended to end-June 2010, although a ceiling was set on such payments. Also addressed was student membership to the general benefits system, and students' rights to apply for benefits after leaving school were enhanced.

On 19 December, Parliament agreed, with Act no. 125/2009, to extend the deadline, set forth in the Act on Financial Undertakings, for initiating cancellation proceedings due to legal instruments of financial institutions in winding-up proceedings from six months to 24 months. The change was made to ensure equitable treatment of creditors in view of the scope of activities of many financial institutions, including those in winding-up proceedings.

On 19 December, Parliament passed Act no. 129/2009, which provides for an environmental and natural resource tax to be levied on fossil fuels, on the one hand, and electricity and hot water, on the other.

On 21 December, Parliament passed Act no. 128/2009 on the generation of State revenues. The main elements of that Act are: i) The standard personal income tax deduction was increased by 4.7% to 530,466 kr. per year and the reference to consumer prices was discontinued. ii) The lowest income tax rate remains unchanged at 24.1%; therefore, the tax-free threshold is raised by the same percentage, to 1,485,000 kr. per year. Income between 2.4 m.kr. and 7.8 m.kr. per year bears 27% income tax, and income over 7.8 m.kr. is taxed at 33%. The tax withholding percentage is based on monthly income. iii) Joint taxation of cohabiting couples was discontinued, except that, if one party earns more than 7.8 m.kr. per year and the other less than that amount, up to half of the income exceeding 7.8 m.kr. may be transferred to the lower-income party. However, the receiving party may not have more than 2.7 m.kr. in the 27% tax bracket. The tax brackets follow the wage index. iv) The tax on individuals' financial income was increased from 15% to 18%; however, 30% of rental income on residential housing and individuals' interest income is exempted, up to 100,000 kr. per year. v) The income tax on legal entities was raised from 15% to 18%. vi) Seamen's credits remain unchanged in 2010 and then are phased out in stages until they are discontinued as of 1 January 2014. vii) The payroll tax rises by 1.6% of the tax base, to 8.65%.

On 21 December, Parliament passed Act no. 137/2009, which provides support for innovation companies. Companies approved by Rannis can deduct 15% of their research and development costs, up to a maximum of 50 m.kr., from their taxable income each operational year. The maximum is set as 75 m.kr. if services are purchased from another approved company. Individuals may deduct the purchase of stock in approved companies from their taxable income, up to a maximum of 300,000 kr. per year.

On 21 December, Parliament passed Act no. 130/2009, providing for various tax measures. The main changes are: i) The oil charge and the gasoline charge increase by 2.50 kr. and 1.65 kr. per litre, respectively. ii) Motor vehicle taxes, alcoholic beverage taxes, and tobacco taxes increase by 10%. iii) The higher value-added tax rate rises from 24.5% to 25.5%. iv) Various fees for permits and services were increased. v) The authorisation to withdraw fund from private pension savings was extended until 1 April 2011, and the maximum withdrawal was raised from 1 m.kr. to 2.5 m.kr.

On 21 December, the first tranche of the loan from the Nordic countries was disbursed to Iceland in connection with the macroeconomic programme of the Icelandic Government and the International Monetary Fund (IMF). The amount disbursed was 300 million euros. The accumulated loan facility authorisation is now 444 million euros. Because there is no further need for borrowed funds at present, 144 million euros will be carried forward to the next period; that is, until after the Second Review of the IMF programme.

On 22 December, the National Budget for 2010 was approved by Parliament. Revenues are estimated at 462 b.kr. and rise by 11% compared to estimated revenues for 2009; expenditures are estimated at 561 b.kr. and declined by 3% compared to 2009 estimates; and the balance on income will be negative by 99 b.kr.

On 22 December, Parliament passed Act no. 138/2009, authorising the Minister of Finance to confirm agreements with the resolution committees of Kaupthing, Glitnir, and Landsbanki concerning their takeover of shares in Arion Bank, Islandsbanki, and NBI.

On 23 December, Fitch Ratings affirmed the Republic of Iceland's sovereign credit rating and removed it from credit watch status. The long-term ratings in foreign and domestic currency are BBB- and A-, respectively. The rating for short-term obligations in foreign currency is F3, and the country ceiling is BBB-. The outlook remains negative.

On 29 December, Parliament agreed, with Act no. 146/2009, to amend legislation on the investigation of the background and causes of the fall of the Icelandic banks in 2008 and related events. The amendments are primarily aimed at preparing for the presentation of the Parliamentary Special Investigative Commission report on the banks' collapse and to clarify what will happen afterwards. In this context, the Commission's deadline for submittal of the report was set at end-January 2010, instructions on parliamentary treatment of the report were added, a provision on storage of and access to the massive electronic databases compiled during the Commission's work was added, and the individuals who worked on the investigation are guaranteed certain immunity from possible legal action arising from their work on the investigation.

On 30 December, Parliament passed Act no. 1/2010 (Icesave), authorising the Minister of Finance to guarantee loans extended to the Depositors' and Investors' Guarantee Fund (DIGF) by the British and Dutch governments, in order to cover payments to depositors of Landsbanki Islands hf.

On 31 December, Standard & Poor's affirmed the Republic of Iceland's sovereign credit rating and changed the outlook from negative to stable following the passage of the Icesave bill. The rating is BBB- for long-term obligations in foreign currency, and BBB+ for long-term obligations in domestic currency. The ratings for short-term obligations in foreign and domestic currency are A-3 and A-2, respectively.