

## Economic and monetary chronicle

### April 2011

On 8 April, the Financial Supervisory Authority announced that it had recalled Askar Capital's, SPB hf.'s and VBS Investment Bank Ltd.'s commercial banking licence.

On 9 April a national referendum was held on Act no. 13/2011 which gave the Minister of Finance the authority to guarantee the repayment by the Icelandic Depositors' and Investors' Guarantee Fund of the British and Dutch governments' cost of the minimum guarantees of deposits in branches of Landsbanki in the United Kingdom and Holland, and to pay the remainder, with interest, of those commitments. The President of Iceland had referred the case to a national referendum on 20 February. The turnout was 75% and the bill was rejected by 59.77% against 40.23%.

On 11 April the Financial Supervisory Authority authorised the transfer of a specified operating part of EA Investment Company hf. (previously MP Bank hf.) to MP Bank hf. (previously nb.is – Savings Bank) and granted the new bank a commercial banking licence. At the same time the company's licence as a savings bank expired. The Financial Supervisory Authority also concluded that Titan Investment Company ehf. was qualified to hold an active share, up to 20%, in the new MP Bank hf.

On 15 April the Central Bank of Iceland, on behalf of the Treasury, offered to purchase, at par, any or all of the foreign-denominated Treasury bonds maturing in 2011 and 2012. The bonds in question were two bond series which were originally in the nominal amount of 1.250 million euros. The offer was an element of the Treasury's liquidity and debt management strategy and the Central Bank of Iceland's reserve management strategy. The invitation stood until 5 May 2011.

On 20 April the Icelandic Competition Authority imposed a per-diem fine on the Central Bank of Iceland in order to force the hand-over of information on individual banks' and savings banks' loans which the Central Bank regarded as confidential information. The fines should amount to 1.5 m.kr. per day until the information was handed over. The fines were cancelled after the lending institutions in question authorised the Central Bank to hand over the requested information.

On 20 April Moody's Investors Service affirmed the Republic of Iceland's Baa3 government bond ratings for domestic and foreign long-term obligations with a negative outlook, following the rejection of the Icesave bill in the national referendum of 9 April. Previously, the rating agency had implied that a rejection of the bill would be likely to result in the lowering of Iceland's ratings. In Moody's announcement on 21 April it was stated that the positive outlook on payments from the old Landsbanki estate, Iceland's performance in the IMF programme and the support of the Nordic governments following the referendum resulted in unchanged ratings.

On 20 April the Monetary Policy Committee of the Central Bank of Iceland decided to keep the Bank's interest rates unchanged. The deposit rate (current account rate) remained 3.25%, the maximum bid rate for 28-day certificates of deposit (CDs) 4.0%, the seven-day collateralised lending rate 4.25%, and the overnight lending rate 5.25%.

### May 2011

On 2 May the Icelandic Authorities handed the EFTA Surveillance Authority a letter from the Minister of Economic Affairs, in which the claim that Iceland had violated the deposit guarantee directive of the European Union was rejected, and the demand made that the case would be withdrawn. It was pointed out that the Landsbanki estate would cover almost all depository claims, disbursements would begin soon and the actions of the United Kingdom and Holland had delayed the settlement.

On 5 May new wage settlements were signed between the national member associations and the largest unions within the Icelandic Confederation of Labour (ASÍ) and the Confederation of Icelandic Employers (SA). The main pillars in the settlements are; a general percentage increase of wages above a certain monthly wage and a króna increase in basic wage rates below that limit, a rise in the minimum wage insurance, and a one off payment to compensate for the delay in reaching a settlement. Similar settlements were also made in other parts of both the private and the public sector. The contracts expire on 31 January 2014, if the assumptions underlying the wage settlements hold. The contracts would have expired on 1 February 2012 if some of the assumptions of the settlements had not been implemented before 22 June 2011. The assumptions underlying the wage settlements that have to be fulfilled upon the review of the contract in 2012 are that; real wages must have increased from December 2010 to December 2011, price levels must have been stable, and the exchange rate of the króna must have strengthened significantly from the signing of the contract up until year-end 2011. Upon the later revision in 2013, real wages must have risen between December 2011 and December 2012, twelve-month inflation must be below 2.5% in December 2012 and the exchange rate index within 190 in that same month. According to the contracts, monthly wages over 282,353 kr. will rise by 4.25% on 1 June 2011, wages over 314,286 kr. by 3.5% on 1 February 2012 and wages over 338,462 kr. by 3.25% on 1 February 2013. Wage rates below these thresholds are to rise by 12 thousand kr. on 1 June 2011 and 11 thousand kr. on 1 February, in both 2012 and 2013. The minimum wage guarantee for full-time work will be 204 thousand kr. per month by the end of the contract time, which is an increase of 23.6%. Employers' expenses will increase only marginally because of the increase in the minimum wage guarantee since these wages only apply to a small minority of workers. The one off payment to compensate for the delay in reaching a settlement is 75 thousand kr., 50 thousand to be paid when the contract had been accepted by members and 25 thousand kr. in connection with holiday and December bonuses in 2011. It is estimated that the gross expenses for employers will be around 13% over the contract period, or around 4.3% on average per

year. Employers' net expenses will be lower since the payroll tax will decrease as unemployment subsidies, according to the Government's statement.

Upon the signing of the wage contracts, the Government announced that personal credit against income taxes would be indexed to the CPI, social security and unemployment benefits would rise in line with wages, income-indexation of child benefits and interest relief would be reviewed, and payroll taxes would be lowered in line with decreases in unemployment expenses. The Government stipulated the expansion of companies' tax environment, reformation of requirements on best practice in business and improvements in employees' position upon bankruptcy. The Government announced that it was its and labour market parties' collective aim for the share of investment of GDP to increase and not to be lower than 20% by the end of the contract period, which amounts to investment being at least 350 b.kr. per year. A campaign to increase study opportunities for the unemployed was promised, with 2 b.kr. to be shifted from unemployment benefits to study opportunities. The Government pledged to work towards the co-ordination of pension rights without compromising the acquired rights of public employees, and to aim for it to be introduced in Parliament before the end of the session. Ultimately, the government promised to show relevant business associations its proposals for changes in the Fisheries Management Act before introducing them in Parliament.

On 6 May the Central Bank announced that it had been decided to purchase, at par value, foreign Treasury bonds for approximately 346 million euros (roughly 57 b.kr.). The bonds will mature in 2011 and 2012. The purchase was the outcome of a tender among investors in Treasury bonds which was announced on 15 April. The two bond series in question were in the original nominal amount of 1.250 million euros (total 204 b.kr.). Prior to the purchase approximately 800 million euros (130 b.kr.) were outstanding.

On 16 May Fitch Ratings revised the outlook for Iceland's ratings to stable from negative.

On 17 May ratings agency Standard & Poor's affirmed the Republic of Iceland's credit rating for foreign obligations. The rating for domestic long-term obligations was lowered to BBB-.

On 23 May the Central Bank offered to purchase Icelandic krónur for cash payment in foreign currency. The auction is an element in the removal of restrictions on movement of capital as set forth in the Central Bank's capital account liberalisation strategy, published on 25 March 2011. The Central Bank offered to purchase 15 b.kr. in return for payment in euros. The objective of these initial measures in Phase I of the capital account liberalisation strategy is to enable investors to sell their króna assets in an orderly manner if they so choose.

## June 2011

On 3 June the Executive Board of the International Monetary Fund completed the fifth review of Iceland's economic programme. It was also agreed to merge the two last reviews into one. Upon the comple-

tion of the review the sixth instalment of the IMF loan, equivalent to SDR 140 million or 26 b.kr., became available.

On 7 June an auction in which the Central Bank purchased Icelandic krónur against cash payment in foreign currency took place. The offer was announced on 23 May. The auction was structured so that all accepted offers were based on the exchange rates submitted. In all, offers were submitted for 61.13 b.kr. and offers amounting to 13.4 b.kr. were accepted. The average accepted price was 218,89 kr. per euro, with the minimum price of accepted offers being 215 kr. per euro.

On 9 June the Treasury completed contracts on the issue of bonds for 1 billion USD, or roughly 114 b.kr. The bonds have fixed interest rates and a maturity of five years with a 4.993% yield, which reflects a 3.20% premium over interest rates in the interbank market. The transaction was well received by investors and demand amounted to 2 billion USD.

On 10 June 2011 Parliament passed Act no. 64/2011 amending Act no. 65/2007, on the emission of greenhouse gases. The amendment incorporates the emission trading system of the European Union into Icelandic law.

On 10 June Parliament passed Act no. 78/2011, amending Act no. 161/2002 on financial undertakings. The amendments strengthen the executive rights of claimants and resolution committees to dispose of assets, strengthen the rights of claimants in other countries regarding termination, make a competence requirement for membership in resolution committees, confirm the Financial Supervisory Authority's rights of surveillance of wind-up committees and resolution committees and stipulate their obligation to inform claimants of all sizable dispositions.

On 10 June Parliament passed Resolution no. 42/139 on the appointment of a committee to investigate the fall of the savings banks.

On 11 June Parliament passed Act no. 70/2011 amending the Fisheries Management Act. The changes increase the share of inshore fishing and allocate an additional quota of several species against payment. Deductions on regional catch quota and inshore fishing will from now on be partly levied on all fishing licences rather than by species types and, in inshore fishing, there will be restrictions on multi-vessel operations. Regional quotas are increased and fishing fee for fisheries in general raised from 9.5% to 13% of its calculated base with 15% of the fee being accrued by municipalities.

On 11 June Parliament passed Act no. 73/2011 which implemented items in the Government's statement in connection with the wage contracts in May.

On 11 June Parliament passed Act no. 81/2011 which extended the provisional authority of the Central Bank of Iceland to limit or stop certain categories of capital movements, and foreign exchange transactions in connection with them, until 30 September 2011.

On 14 June the Financial Supervisory Authority announced the authorisation of the merger of Avant hf. and SP fjármögnun hf. with Landsbankinn hf. under the name of Landsbankinn.

On 15 June the Monetary Policy Committee of the Central Bank of Iceland decided to keep the Bank's interest rates unchanged. The deposit rate (current account rate) remained 3.25%, the maximum bid rate for 28-day certificates of deposit (CDs) 4.0%, the seven-day collateralised lending rate 4.25%, and the overnight lending rate 5.25%.

On 16 June the Central Bank offered to purchase euros against payment in Treasury bonds. The auction was an element in the capital accounts liberalisation. The aim of these measures was to recoup the foreign currency that the Central Bank of Iceland used to purchase offshore krónur in the previous auction and sell krónur to buyers that are prepared to hold them for at least five years. The Central Bank offered to purchase 64 million euros against payment in Treasury series RIKS 30 0701.

On 23 June Registers Iceland presented its annual real estate evaluation, which will be the basis of tax assessment in 2012. The overall evaluation of properties rises by 6.8% and will be roughly 4,400 b.kr. The overall evaluation of residential property rises by 9%.

On 24 June the Financial Supervisory Authority announced it had revoked Keflavík Savings Bank's commercial banking licence due to the ruling of the dissolution of the Savings Bank.

On 28 June the auction that was announced on 16 June took place. Offers were submitted for a total of 71.8 million euros, and offers for 61.74 million euros were accepted. The auction was structured with a single-price format, so that all accepted offers were made available to primary dealers at the same price, which was set at 210.00 kr. per euro. Purchasers received indexed Treasury bonds in the series RIKS 30 0701 as payment for the foreign currency.

### July 2011

On 4 July the Financial Supervisory Authority announced that its Board had passed rules on the wage bonus system of financial undertakings as was stipulated with the amendment to laws on financial undertakings. Annual wage bonuses may not be higher than 25% of annual pay without a bonus, and the disbursement of a portion of the wage bonus shall be delayed by at least 3 years. A wage bonus must be related to performance.

On 5 July the Minister of Fisheries and Agriculture announced his decision on total allowable quota for the fishing year 2011/2012. The allowed quota of cod increases by 17 thousand tons, the allowed quota of haddock decreases by 5 thousand tons, redfish allowances increase by 12 thousand tons and the total of allocated quotas by 32.5 thousand tons.

On 6 July the Central Bank offered to purchase Icelandic krónur in return for cash payment in foreign currency. The auction was an element in the removal of restrictions on movement of capital. The Bank offered to purchase 15 b.kr. in return for payment in euros.

On 12 July the Central Bank announced the results of an auction of foreign currency in return for payment in Icelandic krónur which was

introduced on 6 July. In all, offers were submitted for 52.2 b.kr. and offers amounting to 14.9 b.kr. were accepted. The minimum price of accepted offers was 215.00 kr. per euro but the average accepted price was 216.33 kr. per euro. Offers over the minimum price were accepted in full, and those equal to the minimum price were accepted pro rata, at a percentage of 44.0%.

On 13 July an agreement between Byr and Íslandsbanki was announced in which the bank will provide Byr with new equity and at the same time purchase Byr Resolution Committee's and the Ministry of Finance's share in the savings bank. The companies will then merge under the name of Íslandsbanki, contingent on approval by the Icelandic Competition Authority and the Financial Supervisory Authority.

On 14 July the Parliamentary Ombudsman notified the Central Bank of Iceland of the Icelandic Households' Coalition's opinion that the Bank's Rules no. 492/2001 on indexation lacked legal basis. In Article 13 of Act no. 38/2011 on interest and indexation it is stipulated that the payments of loans should be indexed, rather than their principal as the Rules stipulate. Therefore, it is the Coalition's opinion that financial institutions' collection of indexed claims is illegal. In its reply dated 30 August 2011 the Central Bank pointed out that the Rules were set in accordance with instructions in the Act and that in practice, payments would invariably be the same whether the wording of the Act or the Rules is followed. Thus the Central Bank regulation could not be at odds with the rule of law.

On 15 July the Minister of Fisheries and Agriculture published an ordinance as per recent legislation and increased the fishing fee for the kilo equivalent of cod by 6.44 krónur, to 9.46 krónur. The Treasury's estimated income from the fee increases, from 2.7 b.kr. per year, to 4.5 b.kr. The increase stems from both extended quota permits and the increase in the fishing fee.

On 21 July the Financial Supervisory Authority recalled Glitnir Bank's hf. and Kaupthing Bank's hf. commercial banking licence.

On 26 July the Government Account for the year 2010 was published. The Treasury's expenses in excess of income amounted to 123 b.kr., compared to 139 b.kr. in 2009. Income without interest increased by 13½% due to an increase in tax revenue. Expenses increased by 4% from year to year and exceeded the budget by 7½%. If interest, pension commitments, debt write-offs and other factors connected with the economic crisis of 2008 are overlooked, expenses decreased by 3% in nominal terms and 8% in real terms. By those standards, the Treasury was within the budget.

On 28 July it was announced that the Central Bank of Iceland Holding Company ehf. had completed the sale of a 52.4% share in Sjóvá-Almennar Insurance hf. in accordance with a contract dated 18 January 2011. The buyer was SF1 slhf., a company in the supervision of Stefmir hf. The sale had been approved by the Financial Supervisory Authority and the Icelandic Competition Authority.

**August 2011**

On 2 August the Central Bank of Iceland offered to purchase 72 million euros against payment in Treasury bonds. The auction was an element in the removal of capital controls, as set forth in the capital controls liberalisation strategy dated 25 March 2011. The aim of these measures was to recoup the foreign currency that the Central Bank of Iceland used to purchase krónur in the previous auction and sell krónur to buyers that are prepared to hold them for at least five years.

On 4 August it was noted that the EFTA Court had pronounced that the Icelandic Authorities were unauthorised to stipulate that workers, who are temporarily sent to Iceland, should hold rights which are reserved for Icelandic workers in the Icelandic labour market, if the rights are in excess of the accounted minimum rights of these workers in the relevant EFTA Directive.

On 16 August the Central Bank of Iceland published the results of a foreign currency auction that was announced on 2 August with the auction amount of 72 million euros. Offers were submitted for a total of 3.4 million euros and all offers were accepted in full. The auction was structured with a single-price format, so that all accepted offers were made available to primary dealers at the same price, which was set at 210.00 kr. per euro. Purchasers received indexed Treasury bonds as payment for the foreign currency.

On 17 August the Monetary Policy Committee of the Central Bank of Iceland decided to raise the Bank's interest rates by 0.25 percentage points. The current account rate therefore became 3.5%, the maximum rate on 28-day certificates of deposit (CDs) 4.25%, the seven-day collateralised lending rate 4.50%, and the overnight lending rate 5.5%.

On 26 August the Executive Board of the International Monetary Fund completed the sixth and final review of Iceland's economic programme. The completion of this review enabled the immediate disbursement of an amount equivalent to SDR 280 million which is equal to 51 b.kr. In total, the IMF loan to Iceland amounted to SDR 1.4 billion or 257 b.kr. Additionally the Nordic countries and Poland lent roughly 150 b.kr. in connection with the economic programme, and granted lending facilities of a total of roughly 160 b.kr.

On 31 August it was announced that an agreement had been reached on the acquisition of the consultancy division of Saga Investment Bank by MP bank.

On 31 August the Financial Supervisory Authority granted Straumur IB hf. licence as a credit institution in accordance with legislation on financial institutions.

**September 2011**

On 1 September Arion Bank introduced non-indexed housing loans with maturity of 25 or 40 years. The loans bear an interest of 6.45% up to a 60% loan-to-value ratio and they are fixed for the first five years. Additional loans up to a loan-to-value ratio of 80% bear 7.55%

interest. The interest rates will be re-evaluated in five years in line with market rates. Customers can then decide whether to continue, change their loan format, or pay the loan without pre-payment penalty. Other financial institutions followed suit and offered compatible, non-indexed loans.

On 2 September Parliament passed Act no. 103/2011 amending the Social Security Act and the Act on the Legal Status of Employees upon the Change of Ownership of Companies. A stipulation on the extended duration of income-related benefits in proportion to rights to such benefits as regards a full-time position against used rights of benefits, was extended. Also, it was stipulated that an entity that takes over a company assumes duties towards employees according to current contracts. The amendments were made in connection with the Government's involvement in the wage settlements in May.

On 8 September, the Minister of Fisheries and Agriculture announced an initial quota of 181 thousand tons for capelin vessels for the upcoming season.

On 16 September Parliament passed Act no. 119/2011, amending Act no. 161/2002 on Financial Undertakings, with subsequent amendments (owners' equity, high risk, securitisation etc.). The main purpose of the legislation was to introduce into Icelandic law the content of EU Directive no. 2009/111/EB, but also to make minor changes to other stipulations in the legislation, such as Paragraph 4, Art. 52, on the eligibility of board members of Financial Institutions.

On 17 September Parliament passed Act no. 120/2011 on Payment Services, which legalises the European Payment Service Directive no. 2007/64/EB and sets an integral legislation on payment services. The aim of the directive is to create an integral, coordinated and modern regulatory framework for payment services within the European Economic Area. In the legislation there are for example extensive stipulations on rights and duties of users and providers of payment services.

On 17 September Parliament passed Act no. 122/2011, amending the Act on Mandatory Insurance of Pension Rights and the Operation of Pension Funds. The competence requirements of directors and board members were increased and warranties to withdraw third-pillar pension savings were expanded.

On 17 September Parliament passed Act no. 123/2011, amending the Act on the Mandatory Insurance of Pension Rights and the Operation of Pension Funds. Pension funds were authorised to own and operate residential property, establish companies to operate residential property or enter into contracts with private parties on such operations.

On 17 September Parliament passed Act no. 127/2011, amending the Act on Foreign Exchange, the Act on Customs and the Act on the Central Bank of Iceland, as well as legalising rules previously issued by the Central Bank on capital controls. The mandate for the capital controls is extended until year-end 2013. The duration of related clauses in the legislation on customs and the legislation on the Central Bank of Iceland is extended to the same date.



On 17 September Parliament passed Act no. 128/2011 on mutual funds, investment funds and institutional investment funds. Institutional investment funds thereby fall under older legislation that consequently covers all mutual investment funds. The legislation also incorporates into Icelandic law EU Directive 2007/16/EB on amendments to the directive on mutual investment in transferable securities (UCITS). Other principal amendments are: the constriction of investment authorisations, tightened requirements for the operation of funds and an increased obligation to inform customers.

On 17 September Parliament passed Act no. 134/2011, amending the Act on Housing Affairs, no. 44/1998, with subsequent amendments. With the legislation, the Housing Financing Fund is authorised to offer non-indexed loans, but according to the previous legislation, HFF-securities must be indexed in accordance with the Consumer Price Index. It is also stipulated that interest of indexed HFF-securities shall be fixed for the entire credit period, but that interest of non-indexed HFF-securities can be variable.

On 17 September Parliament passed Local Government Act no. 138/2011. The main changes in local government finances are that budgets and financial statements are to be handed in earlier than before, and deviations from the budget require a supplementary budget. In every three-year period, total expenses of a municipality and its institutions may not exceed regular income for that period and the total of debt and commitments must not be higher than 150% of regular income. Local Governments are given ten years to adjust to the legislation.

On 21 September the Monetary Policy Committee of the Central Bank of Iceland decided to keep the Bank's interest rates unchanged. The current account rate remained 3.5%, the maximum rate on 28-day certificates of deposit (CDs) was 4.25%, the seven-day collateralised lending rate 4.5%, and the overnight lending rate 5.5%.

On 26 September the Financial Supervisory Authority ruled that Íslandsbanki hf. was qualified to handle such a large (active) share in BYR hf., that BYR would become its subsidiary.

On 28 September the Financial Supervisory Authority revoked the collection licence of SPRON Factoring hf., the operating license of Vextir hf.-securities handling as well as, partially, the commercial banking licence of Landsbanki Ísland hf. (the old Landsbanki), due to the ruling of the resolution of the Bank.

