

Economic and monetary chronicle

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 100(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-Burdarás 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 in court cases,
- 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 1,775 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 three-member 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 tonnes 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 Skúla-son, and Katrín Olga Jóhannsdóttir. The following were elected as alternates: Margrét Kristmannsdóttir, Anna Ólafsdóttir Björnsson, Björn Herbert Guðbjörnsson, Guðrún Ágústa Guðmundsdóttir, Birgir Þór Runólfsson, Ingibjörg Ingvadóttir, 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.