



GOVERNMENT DEBT MANAGEMENT

Kalkofnsvegi 1 150 Reykjavik Iceland
phone: 569 9600 fax: 569 9604
email: lanamal@lanamal.is
internet: <http://www.lanamal.is>

Rules on securities lending by the Central Bank of Iceland, on behalf of the Treasury, to primary dealers

These rules are set on the basis of Article 9 of the current agreement between the Central Bank of Iceland, on behalf of the Treasury (hereinafter referred to as the Central Bank), and primary dealers, concerning Treasury bond issuance and market making in the secondary market. According to the agreements, primary dealers have the option of borrowing Treasury securities (hereinafter referred to as loaned securities) from the Central Bank upon submittal of collateral.

Article 1

Duration of loan

Primary dealers may request to borrow securities on any day when the NASDAQ Iceland exchange is open for business, from the market opening until 15 minutes after the market close. The maximum loan period is 28 days; that is, from a given day of the week until the same day four weeks later. If the settlement date falls on a holiday, the maximum loan period shall be reduced and the settlement date moved forward to the last business day on which the securities exchange is open for trading prior to the said holiday. Treasury and Market Operation Department (Government Debt Management) of the Central Bank of Iceland handles interactions with primary dealers concerning securities lending.

Article 2

Credit lines and series

Information on credit lines and series can be found in the Terms and Conditions for Securities Lending to Primary Dealers, which are published on the website www.lanamal.is.

Article 3

Financial collateral arrangements

Financial collateral arrangements for Central Bank securities lending facilities to primary dealers are governed by the provisions of Act no. 46/2005.

The primary dealer shall sign a statement of collateral pledging as collateral all of its financial obligations pertaining to the securities loan granted it by the Central Bank and specifying how the collateral may be appropriated in the event of non-fulfilment.



GOVERNMENT DEBT MANAGEMENT

Article 4

Securities eligible as collateral

Securities eligible as collateral may be the following:

1. Debt instruments issued by the Treasury.
2. Debt instruments issued by the Housing Financing Fund.
3. Cash in Icelandic krónur, according to the decision of the Central Bank of Iceland.
4. Other collateral deemed eligible by the Central Bank of Iceland at any given time.

Article 5

Eligibility requirements for securities used as collateral

1. The securities shall be issued in Icelandic krónur.
2. The securities must be electronically registered in a central depository recognised by the Central Bank.
3. The securities have a market maker on a regulated securities exchange or through recognised data vendors approved by the Central Bank.

In exceptional circumstances, the Central Bank of Iceland may accept securities as collateral even though they do not meet the eligibility requirements set forth in Items 1 – 3 above.

Article 6

Reservations concerning the eligibility of securities as collateral

Primary dealers are responsible for ensuring that securities provided under financial collateral arrangements for securities lending facilities with the Central Bank are free of liens and encumbrances.

Article 7

Payments of principal and interest

In general, securities submitted as collateral shall be selected to exclude those maturing before the expiry of the agreement.

With the approval of the Central Bank, it is permissible to pledge instalments or interest paid during the term of the agreement as collateral. If payment is remitted to the Central Bank on securities held in custody at the Bank, the payment shall be deposited to an account with the Central Bank in the name of the primary dealer and shall be held as a time deposit in that account until the loaned securities have been returned or new collateral submitted. If a primary dealer has borrowed a bond series that pays fixed annual interest, it is required to reimburse the Central Bank for that amount on the interest payment date. Upon payment of interest, the primary dealer may request reimbursement of that portion of the collateral securities that corresponds to the reduction in the final price of the loaned securities due to the interest payment. The Central Bank is entitled to



GOVERNMENT DEBT MANAGEMENT

demand penalty interest if interest is not paid on the interest payment date. Furthermore, the Central Bank is authorised to withhold and sell collateral securities in an amount equal to the interest payment, plus penalty interest and other costs incurred, if the primary dealer has not remitted the interest payment three (3) days after the interest payment date.

Article 8

Valuation of financial collateral

The valuation of securities submitted as collateral shall be based on the bid and ask prices that apply not before the close of last business day before the date of the agreement, including accrued interest and price indexation. The market price shall be based on the best bid for collateral securities and the best asking price for loaned securities.

The haircut from the market price of collateral securities, according to item 1 and 2 of article 4 shall be as follows:

- 2% for securities with less than one year to maturity.
- 5% for securities with one to five years to maturity.
- 7% for securities with more than five years to maturity.

If, during the term of the agreement, the market value of the collateral securities drops in excess of the haircut, the Central Bank is entitled to require additional collateral commensurate with the amount of the reduction in price.

Article 9

Custody of securities

Securities submitted under a financial collateral arrangement shall be registered with a securities depository that has been granted an operating licence pursuant to the Act on Electronic Registration of Title to Securities, no. 131/1997. Securities that are electronically registered in a foreign securities depository recognised by the Central Bank may be submitted as collateral. If securities are registered in a foreign securities depository, they must be deposited with a custodian (account operator) approved by the Central Bank.

Securities registered in an Icelandic securities depository shall be deposited in a securities deposit account (VS account) held by the primary dealer in the Government Re-lending zone and shall be pledged to the Central Bank by means of a special statement of collateral.

Article 10

Requests for securities loans and delivery of electronic assets

Requests for new securities loans shall be received by the Central Bank before 15:45 hrs. if they are to be processed that same day. It is possible to process simple loan agreements (that is, agreements not provided for in Paragraph 2 of this Article) where the delivery of collateral securities and loaned securities is completed before 11:00 hrs. on the next day the Icelandic Securities Depository is open, and post such transactions to the earlier date. Requests for such loans shall be received by the Central Bank before 9:00 hrs. on the day of processing.



GOVERNMENT DEBT MANAGEMENT

If a primary dealer wishes to conclude a new agreement concerning outstanding loaned securities on the settlement date, with or without amendments, the request must be made before 14:00 hrs. if the securities are held by the Icelandic Securities Depository, and before 12:00 hrs. if they are held in a foreign securities depository.

Delivery to the Icelandic Securities Depository shall be considered satisfactorily accomplished when the primary dealer has delivered the collateral securities to the Icelandic Securities Depository account bearing its own national ID number and the Central Bank has transferred the securities to the Government Re-lending custodial account at the Icelandic Securities Depository. Thereafter, the Central Bank delivers the loaned securities to the Government Re-lending suspense account bearing its own national ID number at the Icelandic Securities Depository, where the primary dealer accesses them. If collateral securities to be delivered to the Central Bank have not been received electronically 30 minutes after the market close on the date of the transaction, the Central Bank may cancel the transaction. On the settlement date of the agreement, the primary dealer must first return the loaned securities to the Government Re-lending suspense account at the Icelandic Securities Depository. After the Central Bank has received the loaned securities, the collateral securities shall be delivered to the suspense account bearing the primary dealer's national ID number. The primary dealer shall return the loaned securities before 14:00 on the settlement date, and the Central Bank shall return the collateral securities before 15:00 on the settlement date, provided the loaned securities have been returned.

In addition, the general rule concerning collateral securities that are not registered with the Icelandic Securities Depository is that they are delivered to the Central Bank before loaned securities are despatched.

Article 11

Settlement complications

If the primary dealer does not deliver the loaned securities on the settlement date, the Central Bank is entitled to demand penalty interest on the initial price of the relevant loaned securities until they have been returned. If three days have passed since the agreement expired and the primary dealer has not yet delivered the loaned securities, the Central Bank is authorised to sell the collateral securities on its own account and to charge the primary dealer for all costs and losses incurred. Further provisions concerning the Central Bank's authority to appropriate assets can be found in the statement of collateral that the primary dealer must sign; cf. Article 3 of these Rules.

If the primary dealer has returned the loaned securities but the Central Bank has not returned the collateral securities on the settlement date, the primary dealer is authorised to demand payment of penalty interest, as well as all costs and damages that he has incurred as a result of the transaction.



GOVERNMENT DEBT MANAGEMENT

Article 12

Notices

Notifications from Primary Dealers to the Central Bank of Iceland concerning financial undertakings discussed in these Rules may be sent by e-mail. It is required that the e-mail be sent by a party authorised to obligate the institution concerned. Primary dealers are responsible for parties representing them in interactions with the Central Bank.

Article 13

Commissions and other expenses

The Central Bank's commissions for securities lending are provided for in the "Terms and conditions for securities lending to primary dealers", which are published on the Government Debt Management website, www.lanamal.is.

Should the Central Bank incur any expenses due to the custody of the collateral securities during the term of the agreement, it is entitled to collect these expenses at the beginning of the term of the agreement. An example of such expenses is the custodial fee for HFF bonds held at Euroclear.

Article 14

Exclusion from facilities

The Central Bank of Iceland may, without prior notice, exclude a primary dealer from further facilities in accordance with these Rules if the primary dealer has not complied with the provisions herein.

Article 15

Entry into force

These Rules are based on existing agreement with primary dealers at any given time. The Rules shall remain in effect even if the agreements are amended. When these Rules take effect, the previous Rules on Central Bank of Iceland Securities Lending Facilities for Primary Dealers, dated 16 April 2013, shall expire. These rules shall take effect immediately upon publication.

Reykjavík, 31 March 2015

Treasury and Market Operations Department

Government Debt Management

CENTRAL BANK OF ICELAND

This is a translation of the authoritative Icelandic text. In the event of any discrepancies between the translation and the original Icelandic text, the original text shall prevail.