



Central Bank of Iceland securities lending facilities for primary dealers

Article 9 of the Agreement concerning Issuance of Treasury Notes and Market Making in Government Securities, dated 29 May 2007, which was concluded between the National Debt Management Agency ("NDMA") and primary dealers, states that a primary dealer may borrow Treasury Notes and Bills ("loaned securities") on a temporary basis in exchange for other securities that will be held as collateral ("collateral securities").

On 1 October 2007 the Central Bank of Iceland took over the tasks described in the said agreement, these tasks were previously carried out by NMDA. This means that facilities previously granted by NMDA will now be granted by the Central Bank.

Article 1

Loan period

It is possible to request access to the Central Bank's securities lending facility from the time trading opens at the OMX Nordic Exchange in Iceland (OMX ICE) until 15 minutes after the close of trading. The maximum loan period is 28 days; that is, from a specified day of the week until the same day of the week 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 OMX ICE is open for trading prior to the said holiday.

Article 2

Credit lines and series

Information about credit lines and series can be found in the document entitled: "Fee schedule and limits for securities lending transactions," which is published on the Government Debt Management website, www.lanamal.is.

Article 3

Eligible securities

Securities that are eligible as collateral ("collateral securities") include all electronically registered securities that meet the following requirements:

1. The market value of the issue is more than 3 billion kr., and it is confirmed that this amount has been sold.
2. The issuer has been assigned a credit rating from one of the following three credit ratings agencies – Standard & Poor's, Moody's, or Fitch – and its long-term credit rating is at least A- (Standard & Poor's and Fitch) or A3 (Moody's).
3. There is a structured market making arrangement in place on a regulated securities exchange or a similar institution, and the bonds are denominated in Icelandic krónas.

Subordinated securities may not serve as collateral, nor may an issuer use his own securities as collateral. It is also prohibited to use bonds or bills of an issuer in which the respective financial undertaking has a qualifying holding, cf. Article 40, Paragraph 2 of the Act on Financial Undertakings, no. 161/2002.



Securities used as collateral must be the property of the primary dealer and must be free of liens and encumbrances upon delivery. The Central Bank of Iceland shall hold a lien on the securities during the term of the agreement (the loan period). The registration of the lien shall be handled in accordance with the provisions of Chapter IV of the Act on Electronic Registration of Title to Securities, no. 131/1997.

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

Article 4

Payments of principal and interest

As a general rule, securities presented as collateral shall not mature during the term of the agreement.

It is permissible to use as collateral securities that pay interest or instalments of principal during the term of the agreement, as long as the final maturity date does not fall during the term of the agreement. The primary dealer is entitled to any payments received by the Central Bank of Iceland while the collateral securities for which payments are made remain in the custody of the Bank. The Central Bank is entitled, however, to demand increased collateral in an amount commensurate with the amount of the payment.

If a primary dealer has borrowed a bond series that pays fixed annual interest, he 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 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 5

Valuation of financial collateral

The valuation of securities used as collateral shall be based on the bid and ask prices on the transaction date, 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 shall be as follows:

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

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 6

Commissions and other costs

The Central Bank of Iceland calculates a commission for securities lending transactions. Information on the calculation of commissions can be found in the document entitled "Fee schedule and limits for securities lending transactions," which is published on the Government Debt Management website, www.lanamal.is.

1. The commission is based on the Central Bank's policy interest rate, which is presented and specified as the nominal interest rate. Interest payable on loaned securities is calculated by adding a premium to the policy interest rate, and interest payable on collateral securities is calculated by deducting the haircut from the policy interest rate. The day count rule for calculating interest payable during the term of the agreement is A/360, where A signifies the actual number of days.
2. A processing fee is charged for each agreement concluded.
3. Commissions are paid at the beginning of the term of the agreement.

Should the Central Bank incur any costs due to the custody of the collateral securities during the term of the agreement, it is entitled to collect these costs 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 7

Delivery of electronic shares

Delivery shall be considered satisfactorily accomplished when the primary dealer delivers the collateral securities to the Icelandic Securities Depository account bearing its own national ID number. The Central Bank then accesses the collateral securities and transfers them to its own custodial account at the Icelandic Securities Depository. Thereafter, the Central Bank delivers the loaned securities to the Government Re-lending suspense account 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 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 are delivered to the suspense account under the national ID number of the primary dealer. 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. If the primary dealer wishes to make any changes to the existing agreement, he shall request them before 14:00.

With respect to collateral securities that are not registered with the Icelandic Securities Depository, the general rule is that they are delivered to the Central Bank before loaned securities are dispatched. On the settlement date of the agreement, the collateral securities are dispatched after the loaned securities have been delivered. Simultaneous delivery is also permissible if possible.

Article 8



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 damages incurred. 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 the payment of penalty interest, as well as all costs and damages that he has incurred as a result of the transaction.

Article 9

Notifications

Notifications from lending institutions to the Central Bank of Iceland concerning financial items discussed in these Rules may be sent by e-mail or fax. It is required that the e-mail or fax be sent by a party authorised to obligate the institution concerned. The Central Bank of Iceland emphasises strongly that primary dealers confirm by telephone when an agreement is sent in this manner. Telephone calls related to transactions are tape-recorded.

Article 10

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 he has not complied with the provisions therein.

Article 11

Entry into force

These Rules, which are based on the agreements concluded with primary dealers on 29 May 2007, shall take effect on 31 January 2008. At that time, the previous Rules on securities lending facilities for primary dealers, dated 5 September 2007, shall be abrogated.

Reykjavík ,30 January 2008
International and Market Department
Central Bank of Iceland