

RULES

on Derivatives Transactions in which the Icelandic króna is Specified in a Contract Against Foreign Currency

Article 1

Scope

These Rules apply at the parent company and group level to commercial banks that have been granted an operating licence pursuant to Article 4, Paragraph 1 of the Act on Financial Undertakings, no. 161/2002, with subsequent amendments, as is further specified in these rules.

Article 2

Definitions

Subsidiary: A company falling under the definition of a subsidiary pursuant to Article 1(a), Item 10 of the Act on Financial Undertakings, no. 161/2002.

Capital base: Capital according to Article 84, Paragraph 1 of the Act on Financial Undertakings, no. 161/2002.

Assets and liabilities in foreign currency: Assets, liabilities, and off-balance sheet items in foreign currency, as well as domestic-currency items that are based on foreign currency exchange rates.

Forward position: All transactions in foreign currency that are settled three business days or more after the trade date, including currency swap agreements and other swap agreements.

Parent company: For the purposes of these Rules, a parent company as defined in the Act on Financial Undertakings, no. 161/2002, provided that it is a commercial bank.

Counterparty: A counterparty in forward contracts that is either a financial or a non-financial counterparty as defined in Article 2, Points 8 and 9 of Regulation (EU) no. 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories, which was published in EEA Supplement no. 17 to the Official Journal of the European Union, dated 16 March 2017, pp 412-470, but with the adaptations that follow from Decision no. 206/2016 of the EEA Joint Committee, which is published in EEA Supplement no. 13 to the Official Journal of the European Union, dated 23 February 2017, pp. 63-71; cf. also Article 2 of the Act on OTC Derivatives, Central Counterparties, and Trade Repositories, no. 15/2018; or another type of counterparty than a financial or non-financial counterparty as described above.

Current position in a foreign currency: Assets and liabilities in a single currency, including spot transactions.

Spot transactions: Transactions that are settled no later than two business days after the trade date.

Conglomerate: For the purposes of these Rules, a conglomerate is defined as a group comprising a parent company and subsidiaries as defined in the Act on Financial Undertakings, no. 161/2002, provided that the parent company is a commercial bank.

Commercial bank: For the purposes of these rules, a commercial bank is defined as a financial undertaking that has been granted a licence to operate as a commercial bank pursuant to Article 4, Paragraph 1, Item 1 of the Act on Financial Undertakings, no. 161/2002, with subsequent amendments, and the consolidation to which it belongs.

Article 3

Calculation of forward foreign currency position

Commercial banks are required to calculate their forward foreign currency position vis-à-vis each counterparty, which is based on contracts specifying the Icelandic króna against a foreign currency. Commercial banks are not required, however, to calculate their forward foreign currency position versus other commercial banks that also fall within the scope of these Rules.

The calculation of the forward foreign currency position vis-à-vis each counterparty according to Paragraph 1 shall contain the following items:

1. The position of forward contracts, futures, and currency swaps, insofar as these agreements are not included in the current position. Currency swap agreements and forward contracts shall be treated as an asset in one currency and a liability in the other.

2. The total net delta value of currency options. The delta value shall be calculated as is provided for in the Regulation on Prudential Requirements for Credit Institutions, no. 233/2017.
3. The market value of derivatives contracts in foreign currency other than those specified in Items 1 and 2 above.

Furthermore, the commercial bank shall calculate its gross forward foreign currency position as the sum of the numerical values of all of its forward foreign currency positions vis-à-vis each individual counterparty pursuant to Paragraph 1.

In the calculation of the forward foreign currency position vis-à-vis each individual counterparty, all asset and liability items shall carry a weight of 100%. The commercial bank's long position in a foreign currency is considered positive, and its short position in a foreign currency is considered negative. Financial instruments composed of multiple currencies must be itemised by the weight of each currency, in the currency in question. Amounts shall be converted using the central exchange rate of the Icelandic króna as listed by the Central Bank of Iceland; cf. Article 29 of Act no. 92/2019. Market makers in the foreign exchange market are permitted, however, to use the end-of-day exchange rate.

In calculating the forward foreign currency position, consolidated entities may exclude a subsidiary, subject to prior authorisation by the Central Bank of Iceland, provided that either of the following conditions is satisfied:

1. The activities of the company, irrespective of its stated purpose according to its Articles of Association, do not entail owning or trading any kind of securities, financial instruments other than securities, derivatives, currencies, or other assets.
2. The company is owned by a commercial bank or subsidiary on the basis of Article 22 of the Act on Financial Undertakings, no. 161/2002, irrespective of whether it is a domestic or foreign company.

Authorisations according to Paragraph 4 shall be requested in writing and supported; they are granted only temporarily, for a maximum of 12 months, and expire automatically at the end of the period of validity.

Article 4

Scope of derivatives transactions in which the Icelandic króna is specified in a contract against foreign currency

Derivatives transactions undertaken by commercial banks in Iceland, wherein the Icelandic króna is specified in a contract against a foreign currency, are subject to the following requirements.

1. Commercial banks' forward foreign currency position vis-à-vis each individual counterparty pursuant to Article 3, Paragraph 1 shall never at any time be positive or negative by more than 10% of the capital base.
2. The commercial banks' gross forward foreign currency position pursuant to Article 3, Paragraph 3 shall never at any time exceed 50% of the capital base.

If a commercial bank's forward foreign currency position vis-à-vis each individual counterparty or its gross forward foreign currency position deviates from the limits specified in Paragraph 1, the commercial bank in question shall take steps to eliminate the deviation within a maximum of three business days.

The limits specified in Paragraph 1 shall be calculated based on the capital base according to the commercial bank's most recent financial statements. Commercial banks are authorised to adjust the capital base at the end of the month to reflect exchange rate movements, provided that the Central Bank of Iceland is notified explicitly of such changes. If this authorisation has been used, a corresponding upward or downward adjustment shall be made at the end of each month.

Article 5

Reporting

Commercial banks shall submit to the Central Bank of Iceland a report on derivatives contracts in which the Icelandic króna is specified in a contract against a foreign currency no later than on the fifth business day of each month.

If an individual transaction exceeds 1,500,000,000 krónur, the Central Bank of Iceland shall be notified expressly of the transaction before 10:00 hrs. the following business day. If total (gross) transactions within a single business day exceed 3,000,000,000 krónur, the 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.

shall be notified expressly of the transaction before 10:00 hrs. the following business day. Transactions reported expressly in accordance with the second and third sentences shall also be included in the monthly report according to Paragraph 1.

The Central Bank of Iceland may demand more frequent reports than is specified here.

Article 6

Penalties

Violations of these Rules may be punishable by administrative fines and the penalties set forth in Articles 15 and 19 of Act no. 70/2021.

Article 7

Entry into effect

These Rules, which are set based on the authorisation in Article 6 of the Foreign Exchange Act, no. 70/2021, and have been approved by the Financial Stability Committee, shall take effect immediately. At the same time, the Rules on Derivatives Transactions in Which the Icelandic Króna is Specified in a Contract Against Foreign Currency, no. 756/2021, are abrogated.

Reykjavík, 28 March 2022

Central Bank of Iceland

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