

Proposals of Vilhjálmur Birgisson, who delivered a separate opinion as a member of the Expert Group on the elimination of inflation-indexation of consumer credit

- **Inflation indexation of new consumer credit will be prohibited from 1 July 2014 onwards.**

The following measures will be taken in tandem with this and to mitigate the impact as appropriate:

- **Tax deduction** A tax deduction will be allowed for reduction to the principal/interest during the first years of the loan term while the debt service burden is higher than on inflation-indexed loans. This will enable more people to invest in their own homes and encourages more moderate leveraging than otherwise. This action would be directed primarily at persons buying their first home.
- **Interest-only loans** The availability of a wide variety of housing mortgages, serving the needs of borrowers, will be ensured. It is important that interest-only loans be available. Such loans have a lower debt service burden than traditional instalment loans and are well suited to lower-income borrowers. The non-payment of the principal could be temporary (e.g. for 5-10 years) or for the entire loan term (up to 30 years). The nominal value of the principal will remain unchanged.
- **Personal pension savings** People will be able to utilise their personal pension savings to reduce the loan principal (similar to what is proposed by the working group on Debt Relief).
- **Homeowners' interest benefits** Homeowners' interest benefits will be applied to relieve borrowers' debt service burden and enable the general public to acquire housing without encouraging indebtedness. Interest benefits will be credited towards loans on a monthly basis instead of being paid in cash once a year.
- **Danish system used to finance housing mortgages** The Danish housing mortgage system offers investors security and borrowers low interest rates and high flexibility. Future arrangements for housing mortgages based on the Danish system will offer Icelandic borrowers a credit environment comparable to the best available.
- **Rental market** Circumstances will be created for a rental market providing people with long-term residential security. It is worthwhile to develop a rental market as a long-term solution in parallel to a home ownership market, as investment in own housing does not suit everyone. This aspect is the task of the project management on the future structure of housing affairs, which is to deliver its proposals early in 2014.
- **Protection against oligopoly and extortionate interest rates** Strict rules and supervision will apply to interest rates on housing mortgages, so that banks

will not have free hands to determine interest rates. The oligopolistic Icelandic financial market makes such measures necessary and urgent.

- **The state will issue inflation-indexed bonds** It is appropriate for the state to issue inflation-indexed bonds so that investors will continue to be offered indexed assets even though indexed housing mortgages and consumer loans disappear from the market. This will furthermore ensure that the state have a direct interest in price level stability in the country.

- **Restraints will be applied to the interest rates and indexation of existing inflation-indexed loans**
 - The indexation basis of existing loans will be altered by amending legislation so as to ensure that this will conform to the Central Bank's inflation target.
 - Indexation will be paid as it accrues rather than being added to the principal as is currently the case.
 - It will be ensured that borrowers can convert inflation-indexed loans to non-indexed loans without a pre-payment charge.

- **An investigation will be made of the actual index distortion in calculation of inflation.**
 - Even if inflation indexation of housing mortgages and consumer loans is eliminated, inflation indexation is of major significance in Icelandic society. It is therefore very important to obtain a conclusion as to the actual distortion or skewing which appears in calculations of inflation.
 - As the Treasury is expected to increase its issuance of inflation-indexed bonds, the Treasury has a major interest in ensuring that distortion of inflation does not place additional burdens on taxpayers and promote transfer of assets from the Treasury to lenders and investors.

- **The authorities will have an independent investigation carried out of the Icelandic pension system.**
 - The working group was unanimous on this point and reference is made to the opinion of the majority of the working group on this issue.