What can we learn from the EFTA Court Judgment of 28 January 2013 (case-16/11)

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Deposit guarantee schemes, the analyse of the EFTA judgement, Icesave case.

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Abstract

EFTA Surveillance Authority v Iceland was a case involving Iceland, United Kingdom and Netherlands. There was a dispute between Iceland and those two states because a privately owned Iceland bank *Landsbanki* went bankrupt, the funds of *Landsbanki* were insufficient to reimburse the customers and the Icelandic State paid the legally required deposit guarantees only to the Icelandic customers. It refused to pay the customers of the foreign branches of *Landsbanki* . In the meantime the United Kingdom and the Netherlands repaid their nationals themselves. So these two states pretended Iceland needs to repay these amounts to them.

This case was brought to the EFTA Court by the EFTA Surveillance Authority. The Court cleared Iceland of all charges.

The Iceland doesn't have to sign a sovereign loan guarantee agreement for repayment of the deposit guarantees to the foreign customers but Landsbanki receivership is liable to reimburse the governments who paid to their nationals the (minimum) deposit guarantee foreseen for Icelandic customers.

Introduction:

The EFTA case-16/11 is not only a legal case but also a political one: it is a diplomatic dispute involving Iceland, United Kingdom and Netherlands.

A small countries' bankruptcy had a huge influence on the economy of other states and their citizens that is why it is important to analyse the economic problems and legal solutions to them.

This case is not only recent but also a hot topic nowadays, in 2015, as the receivership is still paying the customers, they should have paid everything before 2017.

I find it important to explain in this paper not only the judgment but also the *Icesave dispute* itself.

The Icesave dispute has been and is still under particular attention of the press; therefore I watched the videos of discussions on TV (news, TV shows) regarding this matter to get a general overview of the problematic. And I used the judgment as well as legal and economical articles on EFTA case and Icesave Dispute.

Methodology

First of all I read the EFTA judgement itself and tried to find and understand all the concepts which are used in it (I put the definitions of the concepts in the footnotes) .Then I read the different articles explaining the main issues (economic, political, legal) which arise in the Icesave dispute.

The second step was elaborating a plan of my paper to cover all the points which, from my point of view, have to be covered in this work.

The third step was to summarise all the information I found and to put it in a coherent structured way.

The forth step is drawing my own conclusions, from the discussion of the findings.

Results (description of the findings)

Firstly, we need to understand what happened in this case. Therefore I will explain the case facts (N.B.: when I am referring to the case term, it means both Icesave dispute as a political issue and the EFTA judgment as a legal issue decision).

Secondly, I will analyse the following issues raised in the Icesave dispute: the national deposit insurance schemes of Iceland, the obligation of result coming from the Directive on deposit-guarantee schemes (94/19/EC), the applicability of anti-terrorism rules to the case / the discrimination based on the nationality, the political complot between the Icelandic politicians.

Case facts precisions

Landsbanki went bankrupt. It had several branches in different countries, United Kingdom and Netherlands. When it happened, the Icelandic customers received part of their savings, as forseen by the minimum deposit guarantees schemes of Iceland. The Icelandic state paid it. But it didn't pay the customers from United Kingdom and Netherlands. Therefore a diplomatic dispute raised: United Kingdom and Netherlands wanted Iceland to pay to its foreign customers at least Icelandic minimum deposit guarantee, by selling assets of Landsbanki receivership. They also asked that Iceland makes a sovereign guarantee of last resort, a repayment guarantee, meaning the state will have to reimburse United Kingdom and Netherlands who reimbursed their nationals although it wasn't a UK or Dutch bank. Therefore there have been three attempts to adopt a so called Icesave [1] bill – a repayment agreement. After the failure to adopt such an agreement (the first one was approved by Iceland but rejected by United Kingdom and Netherlands because new terms on liability limitations were added unilaterally by Iceland, and the second and the third ones were rejected during the referendums organised by the Iceland), the United Kingdom and the Netherlands (as EFTA members) decided to submit this issue to the EFTA Court. N.B.: As the Iceland is not a European Union member state, the case went to EFTA and not to CJEU.

As previously said, there are several legal and economical questions here:

The national statutory deposit insurance schemes.

Preliminary note: Iceland is not an European Union Member State, but it transposed the European Union Directives 94/19/EC and 97/9/EC into Icelandic Law, as it is a part of the European Free Trade Association (EFTA) and therefore of the European Economic Area (EEA).

So the Iceland had a deposit insurance scheme which, in principle, should be compatible with the European Union law. It had the "depositors' and investors' guarantee fund.

That time it was foreseen by the European Union law that these schemes must cover up to €20.000 of deposits per person (foreign branches customers by the European included).

The ESA claimed that the Icelandic deposit-guarantee scheme doesn't cover this amount. That will have to be checked in the discussion of the findings part together with the pertinence and the applicability of this directive to the systemic risk case.

The financial crisis in 2008 in Iceland

Iceland had its financial crisis in 2008, as most of the countries in the world.

Landsbanki went bankrupt but that wasn't the only bank which went bust.

The situation for the Iceland was even worth as it lost totally the access to the financial market for funding.

Iceland was accused of “behaving in a very unfriendly way”, mainly by adopting some legal Acts which give a privilege to the national customers in the repayment of their savings. For this reason an anti-terrorist law was applied against Iceland.

The obligation of result in the EU Directives on the deposit guarantee schemes?

ESA said that there is an obligation of result coming from the Directive and the Icelandic State said it’s not true.

Discussion of the findings: *The Icelandic deposit guarantee scheme*

a) ESA said that Iceland breached the articles 3, 4, 7 and 10 of the Directive because its deposit-guarantee scheme did not cover the amount forseen by the Directive.

The Directive foreseens that in case the deposit-guarantee scheme fails, the state has to repay the debt. Iceland said that its deposit guarantee scheme was compatible with the Directive, but there was a systemic failure, 85% of the Icelandic banking system failed in some days in 2008.

Obligation of results? The Icelandic Government said that the Directive doesn’t impose an obligation of result meaning that in case of failure of the deposit guarantee scheme the state has to compensate, in all circumstances. Moreover, it said that that as that was a systemic risk and compensation is impossible in such case.

Iceland used several arguments to defend itself:

The first one is that the Commission's Impact Assessment previously confirmed that the Icelandic Deposit Guarantee Schemes’ funding was compatible and satisfying the EU norms.

The others arguments concern the systemic risk and provide that no state can afford to cover all the deposits, as in case of systemic failure it would amount at 372% of GDP instead of 83%.

b) Secondly, ESA said that Iceland has breached the Article 4 of the EEA Agreement, because it discriminated foreign customers.

Iceland has passed a law on 6 October 2008, just before the crisis arrived in Iceland, which was basically giving the domestic Icelandic customers the guarantee that all their lost deposits will be covered in case any Icelandic bank goes bust. This law gave this guarantee only to the domestic customers; it said nothing about the foreign ones. The Icelandic government saw that the risk of crisis is imminent and therefore saved its domestic customers by creating a new bank, Nýi Landsbanki (owned fully by the Icelandic state and therefore in case of bankruptcy the state will have more possibilities to save it, with more light procedures, etc.), where it transferred all the domestic assets and liabilities of the Landsbanki.

Landsbanki was then left with very few assets, only those of the foreign customers. It is obvious that it would not be able to repay them with such low assets. And the Icelandic government for sure knew it.

Iceland said it did not discriminate on the grounds of nationality by transferring the domestic depositors to a new perfectly solvent bank and therefore granting them a total repayment in case of bankruptcy.

c) UK parliament reacted on this by applying its anti-terrorism legislation against Iceland, naming the Icelandic government actions an “unfriendly act”. United Kingdom wanted to freeze the Icelandic banks assets in the UK and probably use them to repay the foreign customers of the Landsbanki or, more probably, retain this money until the Iceland makes a repayment agreement to compensate United Kingdom which as said previously reimbursed their nationals.

On 8 October 2008 Landsbanki Freezing Order 2008 was passed. The UK parliament used the Part 2 of the

Anti-terrorism, Crime and Security Act 2001 when it approved this order, because the Treasury said that the action of Iceland was an action taken to the detriment of the United Kingdom's economy.

This is a very rare case; such unilateral sanctions are used very rarely in practice. It put the Iceland in the same list with the worlds' worst terrorists and of course had a huge negative impact on its financial market and its banking system. That can also explain why Iceland had so many difficulties to overcome this crisis.

This sanction seems to have influenced the Icelandic government as they decided to repay their debt.

Conclusions :

The main purpose of this paper was, from only legal point of view, to know whether following the EFTA case on Icesave dispute the customers are really never safe when they save in the foreign bank?

Following the decision of the EFTA Court, the Icelandic government wasn't obliged to repay the debts of a privately owned bank. This decision can not be repealed.

So does it mean that today a Luxemburgish customer of a foreign bank branch in Luxembourg is not fully protected?

Today the amount of guarantee is increased but because of this EFTA judgment the customers have a reasonable fear of putting a big amount of money in the foreign banks branches. This judgement fights legal uncertainty and puts that aside.

But even though the Iceland doesn't have to pay, they decided to repay the debt in full, because of the international pressure on Iceland to provide compensation. It's a state bail out: banks agreed to increase their capital (means their shareholders vote it, etc.), the state helps the bank too but takes its shares for it. The bank gives more short term loans. And the overnight lending between banks evaluates and long term lending becomes possible. So in Iceland there was both bail-in (changing the loans type, increasing of the capital, emergency act of Parliament in 2008 which gave a priority status to all the claims) and bail-out (help from the state treasury). The bail-out is often used by many countries. And there is always the same question: why tax players have to support it and pay the bankers irresponsibility? In this particular case the Iceland decided to pay to Netherlands and United Kingdom, so they are bailing-out a national bank but giving money to foreign citizens, to foreign state indirectly. Moreover Iceland is not even in the European Union yet. Therefore it is not surprising at all that the Icesave bills were rejected twice during the referendums.

So from my point of view there should not be fear of putting money in the foreign bank, as most of the countries, especially the member states of the European Union, are ready to bail-out their banks. In case of failure of one of the member states to bail-out their bank, in application of the principle of solidarity, the European institutions will find a solution and help, as they have already done so many times for Greece…

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[1] Icesave was a special type of online bank savings account in Landsbanki, with a high 6 % earnings rate. It was highly promoted by TV commercials, etc.