Brussels, 14 December 2011
Case No: 70866
Event No: 618446

ORIGINAL

EFTA SURVEILLANCE AUTHORITY

IN THE EFTA COURT

APPLICATION

Submitted pursuant to the second paragraph of Article 31 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice by the

EFTA SURVEILLANCE AUTHORITY

Represented by Xavier Lewis, Director, and Gjermund Mathisen, Officer in the Department of Legal & Executive Affairs, acting as Agents

AGAINST

ICELAND

Seeking a declaration that by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and in the United Kingdom provided for in Article 7(1) of the Act referred to at point 19a of Annex IX to the Agreement on the European Economic Area (*Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes*) within the time limits laid down in Article 10 of the Act, Iceland has failed to comply with the obligations resulting from that Act, in particular its Articles 3, 4, 7 and 10, and/or Article 4 of the Agreement on the European Economic Area.

EFTA SURVEILLANCE AUTHORITY

1 Introduction

1. In early October 2008, the three largest Icelandic banks, Kaupþing, Glitnir and Landsbanki collapsed and were taken over by the Icelandic State. The depositors in the foreign branches of Landsbanki lost access to their deposits. Subsequently, those depositors received no compensation from the Icelandic deposit guarantee fund as required by Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes and the Icelandic State took no action to ensure that they did.

2. An important principle is at stake. A main objective of the Directive is to enhance depositor protection. That objective would be compromised if the Directive were interpreted as only obliging Member States to set up a deposit guarantee scheme without any obligation actually to ensure that the aggrieved depositors are provided with compensation. Depositors need to be able to place trust in the national deposit guarantee schemes established to protect them effectively as required by the Directive in order for the financial sector in the internal market to function properly and to increase the stability of the banking system within the EEA.

2 Relevant EEA law

3. The Act referred to at point 19a of Annex IX to the EEA Agreement (*Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes*) as amended, provides for minimum harmonized rules as regards deposit guarantee schemes.[1]

4. Article 1 of Directive 94/19/EC reads:

> For the purposes of this Directive:

[1] (OJ No L 135, 31.5.1994, p. 5), incorporated into the EEA by Decision of the EEA Joint Committee No 18/94 amending Annex IX (Financial Services) to the EEA Agreement of 19 October 1994.

1. 'deposit' shall mean any credit balance which results from funds left in an account or from temporary situations deriving from normal banking transactions and which a credit institution must repay under the legal and contractual conditions applicable, and any debt evidenced by a certificate issued by a credit institution.

[...]

3. 'unavailable deposit' shall mean a deposit that is due and payable but has not been paid by a credit institution under the legal and contractual conditions applicable thereto, where either:

(i) the relevant competent authorities have determined that in their view the credit institution concerned appears to be unable for the time being, for reasons which are directly related to its financial circumstances, to repay the deposit and to have no current prospect of being able to do so.

The competent authorities shall make that determination as soon as possible and at the latest 21 days after first becoming satisfied that a credit institution has failed to repay deposits which are due and payable;

or (ii) a judicial authority has made a ruling for reasons which are directly related to the credit institution's financial circumstances which has the effect of suspending depositors' ability to make claims against it, should that occur before the aforementioned determination has been made;

4. 'credit institution' shall mean an undertaking the business of which is to receive deposits or other repayable funds from the public and to grant credits for its own account;

5. 'branch' shall mean a place of business which forms a legally dependent part of a credit institution and which conducts directly all or some of the operations inherent in the business of credit institutions; any number of branches set up in the same Member State by a credit institution which has its head office in another Member State shall be regarded as a single branch.

5. Article 3 states:

1. Each Member State shall ensure that within its territory one or more deposit-guarantee schemes are introduced and officially recognized.
[...]

6. Article 4 reads:

> 1. Deposit-guarantee schemes introduced and officially recognized in a Member State in accordance with Article 3 (1) shall cover the depositors at branches set up by credit institutions in other Member States.
> [...]

7. Article 7 reads:

> 1. Deposit-guarantee schemes shall stipulate that the aggregate deposits of each depositor must be covered up to ECU 20 000 in the event of deposits' being unavailable.
> [...]
>
> 6. Member States shall ensure that the depositor's rights to compensation may be the subject of an action by the depositor against the deposit-guarantee scheme.

8. Article 8 reads:

> 1. The limits referred to in Article 7 (1), (3) and (4) shall apply to the aggregate deposits placed with the same credit institution irrespective of the number of deposits, the currency and the location within the Community.
> [...]

9. Article 10 reads:

> 1. Deposit-guarantee schemes shall be in a position to pay duly verified claims by depositors in respect of unavailable deposits within three months of the date on which the competent authorities make the determination described in Article 1 (3) (i) or the judicial authority makes the ruling described in Article 1 (3) (ii).
>
> 2. In wholly exceptional circumstances and in special cases a guarantee scheme may apply to the competent authorities for an extension of the time limit. No such extension shall exceed three months. The competent authorities may, at the request of the guarantee scheme, grant no more than two further extensions, neither of which shall exceed three months.
> [...]

10. Article 4 EEA provides:

> "Within the scope of application of this Agreement, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited."

3 Relevant national law

11. At the material time, Directive 94/19/EC was implemented into Icelandic law by Act No. 98/1999 on Deposit Guarantees and Investor-Compensation Scheme (*lög um innstæðutryggingar og tryggingakerfi fyrir fjárfesta*).[2]

12. Article 1 of Act No. 98/1999 reads:

> *Objective*
> The objective of this Act is to guarantee a minimum level of protection to depositors in commercial banks and savings banks, and to customers of companies engaging in securities trading pursuant to law, in the event of difficulties of a given company in meeting its obligations to its customers according to the provisions of this Act.

13. Article 2 of Act No. 98/1999 reads:

> *Institution*
> Guarantees under this Act are entrusted to a special institute named the Depositors' and Investors' Guarantee Fund, hereinafter referred to as the "Fund". The Fund is a private foundation, operating in two independent departments, the Deposit Department and the Securities Department, with separate finances and accounting, cf. however the provisions of Article 12.

14. Article 3 of Act No. 98/1999 reads:

> *Fund Members*
> Commercial banks, savings banks, companies providing investment services, and other parties engaging in securities trading pursuant to law and established in Iceland, shall be members of the Fund. The same shall apply to any branches of such parties within the European Economic Area

[2] The translation of the Act used here may be found at Act No. 98/1999 on Deposit Guarantees and Investor-Compensation Scheme.

within the States parties to the EFTA Convention or in the Faroe Islands. Such parties, hereinafter referred to as Member Companies, shall not be liable for any commitments entered into by the Fund beyond their statutory contributions to the Fund, cf. the provisions of Articles 6 and 7. The Financial Supervisory Authority shall maintain a record of Member Companies.

15. Article 6 of Act No. 98/1999 reads:

Deposit Department
The total assets of the Deposit Department of the Fund shall amount to a minimum of 1% of the average amount of guaranteed deposits in commercial banks and savings banks during the preceding year.
[...]

16. Article 9 of Act No. 98/1999 reads:

Payments from the Fund
If, in the opinion of the Financial Supervisory Authority, a Member Company is unable to render payment of the amount of deposits, securities or cash upon a customer's demand for refunding or return thereof in accordance with applicable terms, the Fund shall pay to the customer of the Member Company the amount of his deposit from the Deposit Department and the value of his securities and cash in connection with securities trading from the Securities Department. The obligation of the Fund to render payment also takes effect if the estate of a Member Company is subjected to bankruptcy proceedings in accordance with the Act on Commercial Banks and Savings Banks and the Act on Securities Trading.
The opinion of the Financial Supervisory Authority shall have been made available no later than three weeks after the Authority first obtains confirmation that the relevant Member Company has not rendered payment to its customer or accounted for his securities in accordance with its obligations.
[...]

Further specifications regarding payments from the Fund shall be included in a Government Regulation.

17. Article 10 of Act No. 98/1999 reads:

> *Amount payable*
> In the event that the assets of either department of the Fund are insufficient to pay the total amount of guaranteed deposits, securities and cash in the Member Companies concerned, payments from each Department [i.e. the Fund's deposits department and the Fund's securities department] shall be divided among the claimants as follows: each claim up to ISK 1.7 million shall be paid in full, and any amount in excess of that shall be paid in equal proportions depending on the extent of each Department's assets. This amount shall be linked to the EUR exchange rate of 5 January 1999. No further claims can be made against the Fund at a later stage even if losses suffered by the claimants have not been compensated in full.
> Should the total assets of the Fund prove insufficient, the Board of Directors may, if it sees compelling reasons to do so, take out a loan in order to compensate losses suffered by claimants.
>
> In the event that payment is effected from the Fund, the claims made on the relevant Member Company or bankruptcy estate will be taken over by the Fund.

4 The Antecedents

18. The Icelandic Parliament established a Special Investigation Commission (SIC) in December 2008 to investigate and analyse the processes leading to the collapse of the three main banks in Iceland. The SIC delivered its report on April 12 2010.[3] For convenience, Chapters 17 and 18 of the SIC report concerning the depositors's and investors' guarantee fund and deposit guarantees in general are annexed (**Annex A 1 : Chapter 17 of the SIC Report**) (**Annex A 2 : Chapter 18 of the SIC Report**).

19. The Report of the SIC contains a detailed narration of the events leading to the collapse of the banks in Iceland. The Authority will refer to the Report of the SIC below. It does so because the Report permits a greater understanding of the

[3] The Report of the SIC is publicly available at the following website: http://sic.althingi.is/

circumstances surrounding the present proceedings, provides contemporaneous evidence of how the Icelandic authorities considered their position under Directive 94/19/EC and how the response to the collapse of Icesave was coordinated between the Icelandic Government and the Icelandic Guarantee Fund.

20. Reference is not made to the Report of the SIC for the purposes of establishing whether or not the Icelandic Government entered into legally binding commitments with the Dutch and British authorities.

4.1 Before the Crash

21. In October 2006, one of the large three Icelandic banks Landsbanki Íslands hf. ("Landsbanki") launched a branch in the United Kingdom which provided online savings accounts under the brand "Icesave". The fact that the Icesave deposit accounts were located in a branch and not in a subsidiary is significant in two respects. First, deposits in a branch can, according to English law, be moved easily "upstream" from the deposit accounts to the bank's operations in Iceland, whereas deposits in subsidiaries are less mobile.[4] Second, deposits in branches are guaranteed, under the terms of Directive 94/19 as will be made clear below, by the deposit guarantee fund established in the home state of the bank, not by the fund set up in the host state of the branch.

22. It became clear from February 2008 onwards that Landsbanki was in a precarious financial situation. In fact, there was a run on the Icesave accounts in the United Kingdom from February to April 2008 as a consequence of negative press coverage and increased scrutiny by the British financial authorities because of the poor financial situation of Landsbanki.

[4] SIC Report, Chapter 18, p. 38 (all references to the Report of the Special Investigation Commission are to the English language version).

23. Nevertheless, Landsbanki introduced a similar Icesave online deposit branch in the Netherlands which started accepting deposits in Amsterdam on 29 May 2008.[5] The decision to do so is described in the Report of the SIC as "nearly incomprehensible".[6]

24. At the start, those online deposit branches attracted considerable deposits. According to the Report of the Special Investigation Commission, deposits in the Icelandic banks amounted to over ISK 250 billion at the beginning of 2000. By October 2008, the time of the collapse of the big three banks, deposits of others than financial institutions amounted to over ISK 3 100 billion. Over ISK 1 700 billion had been deposited with the overseas branches of the Icelandic banks. By the time the three banks collapsed, about half of their deposits were in foreign currencies and deposited with branches of the banks abroad. [7]

25. Iceland had implemented Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes ("Directive 94/19/EC" or "the Directive") by enacting Act no. 98/1999 on Deposit Guarantee and Investor Compensation Scheme. Both of those measures will be described in greater detail below. Act no. 98/1999 set up the Depositors' and Investors' Guarantee Fund ("TIF") which operated from 1 January 2000. When the TIF began working in 2000 it had assets of about ISK 2.9 billion which represented about 1.2% of bank deposits. The Report of the Special Investigation Commission makes clear that while deposits received by Icelandic banks increased enormously, particularly abroad:

> "no amendments were made to the Guarantee Fund's operating rules, including on obligations regarding payment into or disbursements from the Fund. It should be noted, however, that data available to the Special

[5] SIC Report, Chapter 18, p. 54.
[6] SIC Report, Chapter 18, p. 61.
[7] SIC Report, Chapter 17, p. 1

investigation commission clearly show that the Guarantee Fund's position was repeatedly discussed at government level, primarily in 2008."[8]

26. In accordance with the division of responsibility laid down under Directive 94/19/EC, deposits at the British and Dutch branches of Landsbanki were under the responsibility of the Icelandic TIF, which offered a minimum guarantee of EUR 20 887 per depositor, according to Article 10 of Act No. 98/1999. Iceland did not make use of the option provided for in Article 7(2) of the Directive to exclude certain categories of depositors from the guarantee scheme. From May 2008, Landsbanki opted to take part in the Dutch deposit guarantee scheme to supplement its home scheme. At that time, the minimum guaranteed amount in the Dutch scheme was EUR 40 000 per depositor. This was later raised to EUR 100 000 per depositor.[9] Similarly, the United Kingdom branch had joined the British deposit guarantee scheme for additional coverage. As a consequence, deposits at the British branch over EUR 20 887 per depositor were guaranteed by the British scheme up to GBP 50 000 for retail depositors.

27. According to the Report of the SIC the huge increase in Icelandic bank deposits and the failure of the Icelandic authorities to take adequate measures to ensure even the minimum protection of depositors by the TIF resulted in a number of governments - in particular those of the United Kingdom, Sweden and the Netherlands - to ask questions of the Icelandic Ministry of Business Affairs and the TIF itself about the financial capacity and the operating rules of the Guarantee Fund.[10] There followed extensive exchanges between the authorities of the United Kingdom and the Netherlands in particular and the Icelandic authorities on these issues. Those exchanges are narrated in some detail in pages 107 to 119 of Chapter 17 of the Report of the Special investigation commission. Those exchanges show that the TIF would, if the need arose, make prompt payouts of up to the minimum compensation limit of 20 887 Euros per depositor and that a number of different measures were considered to ensure that the minimum payment could be made.

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[8] SIC Report, Chapter 17, p. 2. Underlining added.
[9] See Annual Report 2008 from the Dutch Central Bank, page 85-86.
[10] SIC Report, Chapter 17, p. 3.

For instance, the acting Permanent Secretary of the Ministry of Business Affairs and Chairman of the Board of Directors of TIF wrote in an email dated 14 August 2008 to the Director of Financial Stability at the United Kingdom Treasury, that:

> "[...] It is absolutely clear according to the law that the fund has to pay out claims up to 20,887 Euros and therefore the Board would always seek a loan to ensure that the scheme pays out to that minimum."[11]

28. Similar communications were sent to the Dutch authorities.[12]

29. The issue of whether the Icelandic state itself would provide the loan mentioned in those written assurances remained unclear until 20 August 2008. On that date the acting Permanent Secretary of the Ministry of Business Affairs and Chairman of the Board of Directors of TIF wrote to the Director of Financial Stability at the United Kingdom Treasury in the following terms:

> "In the event which we find very unlikely, that the Board of Directors of the Depositors' and Investors' Guarantee Fund could not raise necessary funds on financial markets, we assure you that the Icelandic Government would do everything that any responsible government would do in such a situation, including assisting the Fund in raising the necessary funds, so that the Fund would be able to meet the minimum compensation limits."[13]

30. The letter explicitly mentioned that the Central Bank of Iceland would act as lender of last resort with the support of the Icelandic government. The letter concluded:

[11] SIC Report, Chapter 17, p. 110.
[12] SIC Report, Chapter 17, p. 111.
[13] SIC Report, Chapter 17, p. 114.

"We would like to underline that the Government is fully aware of its obligations under the EEA Agreement in relation to the Depositors' and Investors' Guarantee Fund and will fulfil those obligations."[14]

4.2 At the Time of the Collapse

31. On 6 October 2008, Landsbanki's Icesave websites in the Netherlands and in the United Kingdom ceased to work. Depositors of those branches lost access to their deposits.

32. On 7 October 2008, Landsbanki collapsed. The Icelandic Financial Supervisory Authority (the "*Fjármálaeftirlitið*", "the FME") assumed the powers of the meeting of the shareholders of Landsbanki and immediately suspended the bank's board in its entirety. The FME appointed a winding-up committee which took over with immediate effect all authority of the board of directors.

33. However, shortly before the collapse of the big three Icelandic banks and of Landsbanki in particular on or around 6 October 2008, there were further exchanges between the Icelandic and British authorities concerning the capacity of the TIF to meet its obligations. In particular, the Director of Financial Stability at the United Kingdom Treasury wrote again to the Ministry of Business Affairs, on the matter on 5 October 2008. The Permanent Secretary of the Ministry of Business Affairs answered him by a letter dated 5 October 2008 shortly after midnight on 6 October. That response stated:

"Reference is made to the discussions you have had with the Ministry this weekend. If needed the Icelandic Government will support the Depositors' and Investors' Guarantee Fund in raising the necessary funds, so that the Fund would be able to meet the minimum limits in the event of a failure of Landsbanki and its UK branch."[15]

[14] SIC Report, Chapter 17, p. 114.
[15] SIC Report, Chapter 17, p. 116.

34. The Icelandic government then issued two public statements. The first, on 6 October 2008, stated that the Icelandic authorities would guarantee domestic deposits in full:

> "The government of Iceland reiterates that deposits in local commercial banks and savings banks and their local branches will be fully guaranteed.
> Deposits refer to all deposits by general depositors and companies that the guarantee of the deposit department of the Guarantee Fund covers."[16]

35. The second, made by the Icelandic Prime Minister on 8 October 2008, declared:

> "The Icelandic Government appreciates that the British authorities are willing to step in and respond to the immediate concerns of Landsbankinn Icesave accounts.
> [...]
> The Icelandic government reiterates that if necessary the Treasury will support the Depositors' and Investors' Guarantee Fund in raising the necessary funds.
> [...]"[17]

36. On 6 October 2008 the Icelandic Parliament adopted the Emergency Act, Act no. 125/2008. That Emergency Act gave the Icelandic financial supervisory authorities greater powers in the event of a collapse of banks. It also provided that "claims for deposits, pursuant to the Act on Deposit Guarantees and Investor Compensation Scheme" and claims taken over by the Fund become "priority claims" as provided for in Article 112 (1) of the Act on Bankruptcy. Until claims by depositors and the Fund were made priority claims, deposits had the status of general claims when dividing up the bankrupt estate of a bank. Likewise, before the Emergency Act, the claims of the Fund in the event that it paid out compensation to depositors, or claims it otherwise took over, were also claims with a general status. Consequently, the reordering of the status of claims by depositors and their successors in title by the adoption of the Emergency Act

[16] SIC Report, Chapter 17, p. 117.
[17] SIC Report, Chapter 17, p. 118.

significantly improved the status of the Fund in bankruptcy proceedings, increased the chances of greater recovery by the Fund in the bankruptcy proceedings and consequently improved the position of the Fund on capital markets should it need to raise a loan to cover its liabilities.

37. Meanwhile, on the domestic market, the domestic deposits of Landsbanki were transferred to a new bank "new Landsbanki" (now NBI hf.) established by the Icelandic Government. The transfer was made by an FME decision of 9 October 2008 (later amended several times but with no effect on the deposits). Consequently, domestic depositors had access to all their funds at all times.

4.3 The Action and Inaction of the TIF

38. The FME issued an opinion on 27 October 2008 stating retrospectively that on 6 October 2008, Landsbanki's Icesave websites in the Netherlands and in the United Kingdom had ceased to work. The FME concluded that on the same day, Landsbanki was unable to make payment of the amount customers demanded, of certain deposits, in accordance with applicable terms.

39. The statement from the FME triggered an obligation for the Icelandic Depositors and Investors Guarantee Fund to make payments in accordance with Article 9 of the Act No. 98/1999 on Deposit Guarantees and Investor Compensation Scheme, to Landsbanki's customers who did not receive the amount of their deposits.

40. According to Article 10 of Directive 94/19, implemented into Icelandic law by Article 7(1) of Regulation No 120/2000 on Deposit Guarantees and Investor-Compensation Scheme, the payments from the fund should be made no later than three months from the time that the opinion of the FME is available, *i.e.* within three months from 27 October 2008. On 26 January 2009, 24 April 2009 and 23 July 2009, the Minister of Economic Affairs extended the deadline for payouts from the fund, each time for three months, based on Article 10(2) of the Directive (Article

7(4) of Regulation No 120/2000). Thus, the final deadline for payments expired on 23 October 2009.

41. As far as the Authority is aware, the Fund made no payments on or about 23 October 2009 to depositors who had lost access to their deposits.

4.4 The Dutch and British Authorities Step In

42. To avoid a catastrophic run on bank deposits on their markets, the Dutch and British authorities stepped in to protect Icesave depositors.

43. Both the United Kingdom and Dutch authorities organised for depositors at the Landsbanki branches in the United Kingdom and the Netherlands to file claims to the deposit guarantee scheme in each country. The British Government arranged for the pay-out of all retail depositors in full.

44. About 300 000 depositors received in total more than GBP 4.5 billion of which GBP 2.1 billion fell within the responsibility of the Icelandic deposit guarantee scheme, based on the minimum laid down in Article 10 of Act No. 98/1999.[18]

45. On 11 October 2008, the Icelandic authorities and the Netherlands concluded a Memorandum of Understanding stipulating that the Icelandic deposit guarantee fund was under an obligation to compensate each Dutch depositor of Landsbanki Amsterdam branch up to EUR 20 887, that the Netherlands would prefinance the amount required and that the Icelandic State would guarantee the loan.[19] The Icelandic Government asserts that the Memorandum of Understanding was never given any legal effect and was soon withdrawn by the Government.[20]

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[18] See Annual Report and Accounts 2008/09 from the UK Financial Services Compensation Scheme, page 25.

[19] Memorandum of Understanding between the Depositors and Investors Guarantee Fund of Iceland, the Government of Iceland and the Government of the Netherlands dated 11 October 2008, published on Island.is.

[20] Reply of 30 September 2011 to the Reasoned Opinion.

46. The Dutch Government organised the compensation of all depositors up to a maximum of EUR 100 000. Between 11 and 31 December 2008, the Dutch Central Bank paid reimbursements totalling EUR 1.53 billion to 118 000 account holders of the Landsbanki branch in the Netherlands. Of this amount, EUR 1.34 billion was within the responsibility of the Icelandic deposit guarantee scheme.[21]

4.5 Subsequent Negotiations Between the Icelandic, Dutch and British Governments

47. It is not central to the Authority's case whether the Icelandic, Dutch and British governments concluded legally binding agreements or not. Nor is it material whether the Icelandic Government expressly recognised or denied that it had any legal obligations under Directive 94/19/EC. Indeed, it is expressly stated in for example the travaux préparatoires to the Act 96/2009 (Icesave 1) that the official position of the Icelandic Government was that it did not recognise that Directive 94/19/EC imposed any legal obligations on it.

48. The Icelandic government did not conclude with the British government a similar agreement to the Memorandum of Understanding that it had concluded with the Dutch government. Nevertheless, it seemed at that time that it was understood by the three governments that the British and Dutch guarantee funds or governments would prefinance the payments made for the compensation which fell under the responsibility of the Icelandic fund.

49. Indeed, on 15 November 2008, the Icelandic Government confirmed in its Letter of Intent and Technical Memorandum of Understanding to the International Monetary Fund[22] that it was "committed to recognize the obligations to all insured depositors". This commitment was made:

[21] See Annual Report 2008 from the Dutch Central Bank, page 85-86.
[22] Letter of Intent and Technical Memorandum of Understanding from the Government of Iceland to the International Monetary Fund, 15 November 2008, point 9, published on the website of the IMF.

> "[...] under the understanding that prefinancing for these claims (was) available by respective foreign governments and that (Iceland) as well as these governments (were) committed to discussions within the coming days with a view to reaching agreement on the precise terms for this prefinancing".

50. The Icelandic Government then entered into further negotiations with the United Kingdom and the Netherlands for the reimbursements of the pay-outs made by those states to the depositors of Landsbanki, for the parts that were within the responsibility of the Icelandic deposit guarantee scheme. The parties reached two agreements in June 2009. After the Icelandic Parliament approved the agreements with conditions, the parties resumed negotiations and new agreements were concluded in December 2009. However, the law voted by the Iceland Parliament and approving the necessary state guarantees under the agreements was turned down in a referendum in March 2010.

51. The Icelandic, United Kingdom and Dutch Governments renegotiated new agreements, which were concluded in December 2010. The corresponding bill was approved by the Icelandic Parliament in February 2011. But again, the law was turned down in a referendum in April 2011.

52. Since then, there have been no further formal negotiations to secure the reimbursement of the compensation paid out by the Dutch and British authorities which fell under the responsibility of the Icelandic deposit guarantee fund.

EFTA SURVEILLANCE AUTHORITY

5 The Administrative Procedure

5.1 The Letter of Formal Notice and its Reply

5.1.1 The Letter of Formal Notice of 26 May 2010

53. On 26 May 2010, the Authority sent a letter of formal notice to Iceland for its failure to ensure that Icesave depositors in the Netherlands and the United Kingdom receive payment of the minimum amount of compensation provided for in Article 7(1) of the Act referred to at point 19a of Annex IX to the EEA Agreement (*Directive 94/19/EC*) as amended within the time limits laid down in Article 10 of the Act, in breach of the obligations resulting from the Act and/or of Article 4 of the EEA Agreement (**Annex A3: Letter of Formal Notice of 26 May 2010**).

54. In particular, the Authority claimed that Iceland had obligations of result to ensure that a deposit guarantee scheme is set up capable of guaranteeing the deposits of depositors up to the amount laid down in Article 7(l) of the Directive and ensure that duly verified claims by depositors of unavailable deposits are paid within the deadline laid down in Article l0 of the Directive.

55. The Authority also stated that the "exceptional circumstances" could not release Iceland from its obligations under the Directive.

56. Finally, the Authority stated that the actions of the Icelandic government left the depositors in the foreign branches of Icesave without any protection under the Directive while domestic depositors never lost access to their deposits and were given a complete guarantee constituted indirect discrimination on the basis of nationality prohibited by Article 4 of the EEA Agreement.

57. Initially, Iceland was requested to submit its observations within two months following receipt of that letter. At the request of the Government of Iceland, the

Authority granted extensions of the deadline, first until 8 September 2010, then until 7 December 2010 and finally until 2 May 2011.

5.1.2 The Reply of 2 May 2011

58. The Government of Iceland answered the letter of formal notice on 2 May 2011 (**Annex A4: Reply from Iceland of 2 May 2011**). In that reply, the Government continued to claim that it is not in breach of its obligations under Directive 94/19/EC and under Article 4 of the EEA Agreement.

59. Iceland's response can be summarised as follows:

- It had fully transposed the Directive into Icelandic law with the adoption of Act No. 98/1999 on Deposit Guarantees and an Investor Compensation Scheme, and following that, established a deposit-guarantee scheme as required.

- The Directive does not impose an obligation of result on the Member States as that would lead inter alia to a *de facto* state guarantee for all deposits amounting to EUR 20 887 for each account in each and every bank.

- The concept of obligation of result in EU law is unclear and does not suffice as legal basis for imposing a duty on Member States which would jeopardise their financial stability. An obligation of result can only materialise - or be breached - once it becomes clear that the actions of a Government did not suffice to ensure the minimum protection for deposits guaranteed by the Directive.

- Iceland ensured - to the extent possible while dealing with a complete collapse of a banking system - that all retail depositors in the failed Icelandic banks would receive compensation in the form of payments from the estates of those banks. Deposit claims were granted priority ranking

when the collapse became unavoidable, thus making up for the obvious shortcomings of any Deposit-guarantee scheme in the event of a total banking system collapse.

- The depositors received compensation from the British and Dutch authorities in any event and that compensation exceeds the minimum deposit guarantee.

- In any event, any breach of the Directive should be considered justifiable in view of the fact that no deposit-guarantee scheme envisioned by the Directive could have dealt with a financial crisis of the magnitude experienced in Iceland in the autumn of 2008.

- Furthermore, any breach committed by Iceland is justified by the various unilateral actions undertaken by the United Kingdom and the Netherlands governments in breach of the EEA Agreement against Landsbanki, the Icelandic state, and other Icelandic interests and their effect on the Government's reaction to the crisis. Those actions obstructed the Icelandic Government's efforts to efficiently reorganise and wind-up Landsbanki to facilitate payments under the deposit guarantee scheme, which efficiency under normal circumstances is now historically evident by the swift resolution of the Kaupthing Edge internet depositor's payment from the estate undisturbed by the German Government. These ill-advised and disproportionate actions justify any breach which the Government may have committed as a consequence.

- Iceland did not discriminate based on nationality, as all non-domestic depositors in Icelandic branches received the same treatment as Icelandic depositors. The difference in treatment related to the location of the deposits and not the nationality of depositors. Furthermore, the situation of depositors of domestic branches, on the one hand, and depositors of the branches abroad, on the other hand, were by all objective measures

incomparable. However, should these measures be found to have been discriminatory in some respect, they were fully justified by having a legitimate aim and passing the test of proportionality.

- Finally, *force majeure* comes into play when assessing the unforeseeable, dire and exceptional circumstances of the case and the Government's inability to fulfil the obligations of the Directive.

5.2 The Reasoned Opinion and its Replies

60. The Authority was unconvinced by the reply to the letter of formal notice. Consequently, it delivered a reasoned opinion to Iceland on 10 June 2011 (**Annex A 5 : Reasoned Opinion of 10 June 2011**.)

5.2.1 The Reasoned Opinion

61. The Authority's reasoned opinion of 10 June 2011 contained essentially the same claims and conclusions as the letter of formal notice of 26 May 2010. It concluded that by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and in the United Kingdom provided for in Article 7(1) of the Directive 94/19/EC within the time limits laid down in Article 10 of the Act, Iceland has failed to comply with the obligations resulting from that Act, in particular Articles 3, 4, 7 and 10, and/or Article 4 of the Agreement on the European Economic Area.

5.2.2 The Replies to the Reasoned Opinion

62. Iceland replied to the reasoned opinion on 30 September 2011 (**Annex A 6 : Reply of 30 September 2011 to the reasoned opinion**).

63. Iceland's reply is in two parts. The first describes the recent developments in the winding up procedure of Landsbanki and the distribution of assets to the

depositor creditors. The reply states that the expected rate of recovery has improved significantly and there is much more certainty on the value of the assets. It states that a first interim payment will be made shortly from the bankruptcy estate which should amount to about ISK 400 billion.

64. The second part of the reply deals with the substantive arguments that the Authority had set out in its letter of formal notice. In its reply, Iceland continues to claim that the Authority is wrong that the Directive imposes an obligation of result. Iceland claims that is made clear by an EC Commission Staff Working Document which shows, according to Iceland that no deposit guarantee fund is designed or intended to cope with a systemic failure of the banking system and that the Directive does not oblige member States to step in and finance the deposit guarantee fund. Iceland also continues to claim that its behaviour does not amount to indirect discrimination prohibited by Article 4 of the EEA Agreement.

65. The reply also contains a confidential annex comprising a provisional decision of the Board of the TIF dated 8 September 2011. That provisional decision was adopted to enable the TIF to disburse such funds as it has to depositors pursuant to Act no. 98/1999. The decision concedes that the TIF will not be able to pay all depositors' claims in full.

66. Iceland sent a further letter dated 13 December 2011 giving more information on the winding up of the Landsbanki estate and describing recent judgments of the Icelandic Supreme Court concerning the reordering of the priority of creditors in that winding up. (**Annex A 7 : Letter from Iceland of 13 December 2011**).

6 The Authority's submissions

67. Iceland has made a number of allegations in its reply of 2 May 2011 concerning what it claims to be a number of breaches of cross-border banking legislation by the United Kingdom and the Netherlands, alleged incorrect implementation of

the Directive by other EEA States and the alleged role of EEA States in the circumstances leading up to deposits becoming unavailable on 6 October 2008 or the recovery rate of the estate of Landsbanki. Breaches by other EEA States have no legal bearing on the present case. Even if such allegations were well founded, they cannot release Iceland from its obligations under Directive 94/19/EC and under Article 4 of the EEA Agreement. According to the Court of Justice's settled case-law, a Member State cannot plead failure to respect the principle of reciprocity or rely on a possible infringement of the Treaty by another Member State to justify its own default[23]. Similarly, the Court of Justice has consistently held that a Member State may not, under any circumstances, unilaterally adopt, on its own authority, corrective or defensive measures designed to obviate any such failure, but is bound to act within the context of the procedures and legal remedies laid down to that effect by the Treaty[24]. The same principles, the Authority submits, apply in EEA law. Consequently, the Authority will not examine the substance of those allegations further.

68. The present infringement proceedings only relate to the compliance, by Iceland, with the obligations it has subscribed to under the EEA Agreement, according to which all depositors whose deposits in branches of Icelandic banks became unavailable must be compensated according to the terms of the protection laid down by Directive 94/19/EC and without discrimination.

69. The Authority is aware that depositors or their successors in title have received partial payment of their claims through payments from the estate of Landsbanki in the course of the pending winding up proceedings. According to Iceland, full reimbursement of those claims will not take place until the end of 2013.[25]

[23] Case C-131/01 *Commission v Italy* [2003] ECR I-1659, paragraph 46; Case C-38/05 *Commission v Ireland*, unpublished, paragraph 17; Case C-266/03 *Commission v Luxembourg* [2005] ECR I-4805, paragraph 35.
[24] Case 232/78 *Commission v France* [1979] ECR 2729, paragraph 9 and Case C-5/94 *Hedley Lomas* [1996] ECR I-2553, paragraph 20.
[25] The letter from Iceland of 13 December 2011 (Annex A 7) merely assumes that final payment from the winding up will be made on 31 December 2013 (Appendix A, page 5 of the letter).

70. Those payments made in the winding up process are very different in nature from the payments that should have been made by the TIF pursuant to Directive 94/19/EC. Indeed, the very purpose of Directive 94/19/EC is to establish a separate procedure allowing depositors to receive rapid payment of the amounts guaranteed without having recourse to lengthy and complex winding up procedures. As the Commission states in its Staff Working Document of 12 July 2010, Document SEC(2010) 834 final,[26] :

> "The existence of [deposit guarantee schemes] also means that most depositors (those who are fully covered) do not have to participate in lengthy insolvency procedures which usually lead to insolvency dividends representing only a fraction of the original claims."

71. The Authority remains of the view set out in its letter of formal notice of 26 May 2010 and in its Reasoned Opinion of 10 June 2011 that Iceland is in breach of its obligations under Directive 94/19/EC and under Article 4 of the EEA Agreement. The Authority considers that Directive 94/19/EC imposes obligations of result on the EFTA States:

1. To ensure that a deposit guarantee scheme, capable of guaranteeing the deposits of depositors up to the amount laid down in Article 7(1) of the Directive[27], is set up, and

2. To ensure that duly verified claims by depositors of unavailable deposits are paid within the deadline laid down in Article 10 of the Directive.

72. The Authority submits it is clear from the wording of Directive 94/19/EC itself that the Directive imposes an obligation of result on the states.

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[26] At page 5, available publicly at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=SEC:2010:0834:FIN:EN:PDF

[27] That provision remains unchanged in the EEA as Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay (OJ 2009 L 68, p. 3) has not been made part of the EEA Agreement to date.

73. Article 3 of the Directive requires the EFTA States to introduce and officially recognise one or more deposit guarantee schemes, which under the terms of Article 7 must cover deposits up to EUR 20 000. The wording of Article 7(1) is unconditional.[28]

74. Article 10(1) of Directive 94/19/EC then requires the EFTA States to ensure that if deposits become unavailable, the necessary procedures are completed no later than three months after the date on which the competent authorities determine that the credit institution concerned appears to be unable to repay the deposit. This deadline may be extended in order to take into account exceptional circumstances, but even in that case, the procedures cannot go beyond 12 months after the recognition of the unavailability of the deposits. The wording of Article 10(1) is also unconditional.

75. The Directive thus imposes upon EFTA States an obligation to ensure compensation of depositors up to at least EUR 20 000 in the event of their deposits being unavailable, irrespective of the reasons for that being the case. The Directive provides for no derogation or exemption from that obligation.

76. That interpretation of the Directive is consonant with the Opinion of an expert group appointed following a meeting of the Finance Ministers of the EU Member States and the EFTA States in November 2008. The group was set up to give an opinion on the position of Iceland and the Directive. That group, comprising representatives of the Council of the European Union, the European Commission, the European Central Bank and the Authority,[29] concluded on 7 November 2008 (**Annex A 8 : Opinion of an expert group of 7 November 2008**) that:

[28] The only limits the EFTA States may impose on the absolute requirements of the first paragraph of Article 7 are strictly circumscribed in paragraphs 2 and 4 and only relate to the possible exclusion of certain types of deposits from the coverage and the possibility to limit coverage to 90%. Iceland has never availed itself of these options.

[29] The opinion makes clear that the representatives gave it in their "personal capacity" and that the opinion "does not commit their respective appointing authorities." No representative of the EFTA states participated in the group.

"[...] Iceland has to ensure that the depositors are treated in compliance with the EEA Agreement, including the Deposit Guarantee Directive, which requires that deposits are repaid up to at least 20.000 EUR for each depositor when deposits become unavailable, regardless of whether their deposits are held in Iceland or at a branch of an Icelandic bank in another EEA State. Iceland should take all appropriate measures to ensure respect of the provisions of the EEA Agreement."

77. That obligation has also been confirmed explicitly by the Court of Justice.

78. In Case C-222/02 *Paul and others*, the Court of Justice held that Directive 94/19:

"[prescribes that] compensation of depositors is ensured in the event that their deposits are unavailable".[30]

79. According to the Court, the Directive gives a right to depositors to a refund of at least EUR 20 000 each, wherever deposits are located in the EU, in the event of the unavailability of deposits.[31] Although the Court did not have to rule specifically on the matter because of the specific facts of the case, it is evident from the judgment that the Court considers the provisions of Articles 7 and 10 of Directive 94/19/EC require a clear and precise result to be achieved.

80. Iceland, in its replies of 2 May 2011 and 30 September 2011, claims both in principle and in the circumstances of this case, that the Authority is wrong to submit that Directive 94/19/EC lays down an obligation of result that it must achieve. In particular, Iceland claims :

- Articles 7 and 10 of Directive 94/19/EC do not lay down an obligation of result;
- Iceland has fully and correctly transposed Directive 94/19/EC;
- Directive 94/19/EC requires no state guarantee or additional liability.

[30] Case C-222/02 *Paul and others* [2004] ECR I-9425, paragraph 30.
[31] Case C-222/02 *Paul and others* [2004] ECR I-9425, paragraphs 26 and 27.

81. The Authority will deal with each of those submissions made by Iceland in turn.

6.1 Obligation of result under Articles 7 and 10 of Directive 94/19/EC

82. In its replies, Iceland claims that Directive 94/19/EC does not provide for an obligation of result as submitted by the Authority. Iceland submits that Article 7 of Directive 94/19/EC imposes no obligation on the state but only an obligation on the deposit guarantee fund. It points out that the EU legislator felt the need to clarify Article 7 of Directive 94/19/EC through Directive 2009/14/EC[32] and explicitly indicate that "*Member States shall ensure that the coverage for the aggregate deposits of each depositor shall be at least EUR 50 000 in the event of deposits being unavailable*".[33]

83. The Authority disagrees. Nothing in the recitals of Directive 2009/14/EC or in the preparatory work leading up to its adoption would suggest that the legislator intended to introduce any substantive changes to Article 7 of the Directive.

84. The fact that the EU legislator appears to have felt the need to underline that the obligations set out in that provision of the Directive were addressed to the states, does not mean that, objectively, those obligations were not stated in a clear and precise fashion prior to the amendment, as determined by the Court of Justice.

85. Indeed, Article 7 of the EEA Agreement provides that the Acts in the Annexes are binding upon the *Contracting Parties*, who under item b) of the Article are left the choice of form and method of implementation of directives. This provision of the EEA Agreement is modelled upon what is now Article 288(3) TFEU which provides that "*A directive shall be binding, as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national authorities the choice of form and methods*". By definition, the obligations set out in directives are

[32] Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay (hereafter "Directive 2009/14/EC"). As indicated above, Article 7 of the Directive remains unchanged in the EEA as Directive 2009/14/EC has not been made part of the EEA Agreement to date.
[33] Letter from the Icelandic Government to the Authority dated 2 May 2011, page 16-17.

addressed to states and not to the bodies that states might be obliged to establish or designate in order to comply with their obligations under those directives. Thus, the change in the wording of Directive 2009/14/EC referred to by the Icelandic authorities makes no substantive change as regards the legal obligations laid down in that provision.

86. The obligation of result imposed by Directive 94/19/EC is clear not just from its wording but also from its context and the objectives it pursues, elements which must be taken into account when interpreting a provision of EU/EEA law.[34]

87. According to its preamble, Directive 94/19/EC seeks to ensure a high level of protection of retail deposits paid into bank accounts within the common market. In particular, recitals 8 and 9 to the Directive set out as its objectives that deposit-guarantee schemes must intervene as soon as deposits become unavailable and must, within a very short period, ensure payments. As stated by the Court of Justice in *Germany v Parliament and Council*, the reduction in the level of protection that may result in certain cases "*does not call into question the general result which the Directive seeks to achieve, namely a considerable improvement in the protection of depositors within the Community.*"[35]

88. Iceland also argues that in *Germany v Parliament and Council*, the Court of Justice, in the context of a plea regarding the legal basis of Directive 94/19/EC, ruled that the objective of the Directive is to abolish obstacles to the right of establishment and the freedom to provide services and that depositor protection is only an incidental effect.[36]

89. It is correct that, in its judgment, the Court of Justice noted that the Directive's aim was "*to promote the harmonious development of the activities of credit institutions throughout the Community by eliminating any restrictions on freedom of establishment and the freedom to provide services, while increasing the stability of the banking system*

[34] Case C-156/98 *Germany v Commission* [2000] ECR I-6857, paragraph 50, and Case C-306/05 *SGAE* [2006] ECR I-11519, paragraph 34.
[35] Case C-233/94 *Germany v Parliament and Council* [1997] ECR I-2405, paragraph 48.
[36] Letter from the Icelandic Government to the Authority dated 2 May 2011, page 13-14.

and the protection of savers"[37]. And indeed, the Court ruled that the Directive's objective is to remove obstacles to free movement of credit institutions across the internal market.

90. But the Court did not rule that the protection of depositors was of incidental effect. On the contrary, the Court of Justice made it clear in the passage quoted above that the protection of depositors is central to the scheme and aim of the Directive.

91. The Court expressly stated that the Directive provides for the compulsory participation by all credit institutions in guarantee schemes providing cover up to EUR 20 000 for the aggregate deposits of each depositor with a credit institution in the event of deposits being unavailable. It noted also that the deposit-guarantee systems introduced by a Member State in accordance with Article 3(1) of the Directive are to cover depositors in branches set up by credit institutions in other Member States. Consequently, the aim and purpose of the Directive is to oblige Member States to introduce a uniform standard of minimum protection of depositors throughout the internal market, so that Member States would no longer be able to invoke depositor protection in order to impede the activities of credit institutions authorized in other Member States[38].

92. Clearly, the system laid down in Directive 94/19/EC rests on the protection of depositors by the schemes of the home state of credit institutions, both for deposits made in the home state and for the deposits made in branches of those credit institutions in other Member States. For such a trans-European cross-border network of protection of depositors to function and safeguard financial stability, EEA States and the depositors in all those EEA States must be able to trust that, whichever credit institution they choose, they will be protected, at the same level.

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[37] Case C-233/94 *Germany v Parliament and Council* [1997] ECR I-2405, paragraph 13. See also the first recital in the preamble to the Directive.

[38] Case C-233/94 *Germany v Parliament and Council* [1997] ECR I-2405, paragraphs 17 to 19.

93. It is doubtful that Member States would have accepted to adopt a harmonising directive and thereby renounce their right to restrict the activities of credit institutions established in other Member States with insufficient depositor protection, simply on the basis of a formal obligation, for all Member States, to establish some kind of deposit guarantee scheme. The aim of a credible trans-European cross-border network of protection of depositors, which is an indispensible condition for a cross-border single market of credit institutions, can only be safeguarded by a clear and unconditional requirement that, within a specified deadline, a certain amount will be paid out in the event of a bank failure. Which is why Articles 7 and 10 impose an obligation of result, which alone can ensure the credibility of the system and thus allow a well functioning single market for credit institutions.

94. Accordingly, the Authority submits that the Directive imposes an obligation of result on the Icelandic Government, which is to ensure that a deposit guarantee scheme, capable of guaranteeing the deposits up to the amount laid down in Article 7(1) of the Directive, is set up, and to ensure that duly verified claims by depositors of unavailable deposits are paid within the deadline laid down in Article 10 of the Directive.

95. It makes no difference to the Authority's conclusion on this issue whether, as in this case, the authorities of other EEA States have stepped in to compensate depositors of foreign branches. Iceland claims in its letter of 13 December 2011 that the Directive only creates rights for individual depositors, not for governments.[39] The Authority submits that Article 4 of the Directive clearly provides that a deposit guarantee fund set up in an EEA State must cover depositors at branches set up by banks in other EEA States. Iceland did not ensure that the depositors in Icesave received compensation from the Icelandic Fund: it is that breach of the Directive which is directly attributable to Iceland. It is immaterial to the breach committed by Iceland that the British and Dutch

[39] Letter from Iceland of 13 December 2011, page 4.

authorities intervened to provide compensation to depositors and seek reimbursement of the sums they had paid out.[40]

96. According to the information available to the Authority, following the unavailability of Icesave deposits on 6 October 2008, the FME issued its finding of unavailability of deposits regarding those deposits on 27 October 2008. That was the first step of the procedure laid down in Article 10(1) of Directive 94/19/EC. According to the Directive, the time-frame foreseen for the necessary procedure shall not exceed three months following the finding of unavailability of deposits by the competent authorities, unless the deposit guarantee scheme requests the competent authorities to extend that time limit[41]. The Icelandic authorities extended the deadline for payment until 23 October 2009[42]. Subsequently, however, further steps were not taken and, in particular, the relevant procedures foreseen under national law were not completed.

97. The Authority submits that the Fund forms part of the Icelandic State within the meaning of the EEA Agreement. Indeed, it was established by law with the sole purpose of providing a public service, it acts within a tightly defined framework which leaves no genuine margin for independent decisions by its board and it has special powers beyond those which result from the normal rules applicable in relations between individuals.[43]

98. Even if the Fund were considered to be an independent entity, the state remains under the obligation to ensure full compliance with the Directive and proper compensation of depositors under its terms.

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[40] In fact, wholesale depositors were not covered by the British scheme whilst they were in principle covered by the Icelandic scheme. Consequently not all depositors in Icesave who could have been compensated by the Icelandic Fund if they lodged claims have received compensation from the British scheme.

[41] Article 10 of Directive 94/19/EC.

[42] http://www.tryggingarsjodur.is/Frett/9747/

[43] Case C-356/05 *Elaine Farrell v. Alan Whitty and Others* [2007] ECR I-3067, paragraph 40 and the cases cited therein. Furthermore, Case C-157/02 *Rieser Internationale Transporte GmbH v. Asfinag* [2004] ECR I-1477, paragraphs 24-28. This case law deals with whether the bodies in question are part of the State for the purposes of determining whether provisions of directives having direct effect may be relied on against those bodies. EEA law does not provide for direct effect, Case E-1/07 *Criminal proceedings against A* [2007] EFTA Court Rep. p. 246, paragraph 40. However, the Authority considers that this case law is relevant with regard to determining which bodies fall to be regarded as emanations of the State for the purposes of EEA law.

99. Moreover, the facts of this particular case show that the Fund and the Icelandic administration were linked to a degree that they cannot be considered to be wholly separate entities. It is noted in Chapter 17 of the Report of the SIC that:

> "Since the establishment of [the Fund] and until the failure of the big Icelandic banks at the beginning of October 2008, an agreement was in force between the Fund and the Central Bank of Iceland specifying that an officer of the CBI should be employed as the Fund's managing director."[44]

100. Chapter 17 of the Report of the SIC also makes clear that the Ministry of Business Affairs exercised supervision of the activities of the Fund and appointed staff members to the post of Chairman of the Board of Directors of the Fund.[45]

101. The Report of the SIC concludes on this matter in the following terms:

> "The Minister of Business Affairs, in accordance with Article 4 of the Act no. 98/1999, appointed the Chairman of the Board of Directors of the [Fund]. Even though it did not derive directly from the aforesaid Act, the minister adhered to the custom of appointing an employee of the Ministry of Business Affairs as chairman, as had been done since the Fund was established. One can only conclude that this led in practice to significant and close collegial relations being established between the Ministry and the [Fund], and in fact decreased the independence and efficiency of the Board of Directors of the Guarantee Fund. Leadership in matters concerning the Fund had, therefore, rested with the Ministry of Business Affairs to a greater extent than with the Board of the Fund as such, including representatives of the credit institutions.
>
> [...]
>
> The situation was, therefore, that the Chairman of the Board of Directors of the Guarantee Fund was simultaneously involved in demanding that the Icelandic government clarify its position regarding its intentions on account of the

[44] Report of SIC, Chapter 17, p. 30.
[45] Report of SIC, Chapter 17, p. 66.

Fund's obligations, and responding to inquiries from foreign parties about the Fund's affairs and obligations, either in the name of the Ministry or on behalf of the Guarantee Fund."[46]

102. As a consequence, any breach of the Directive by the Fund is attributable directly to the Icelandic State both in law and in fact.

103. As the Icelandic State, neither directly nor through the Fund, has ensured payment to those depositors in the Netherlands and the United Kingdom whose deposits became unavailable within the meaning of Directive, Iceland has failed to comply with its obligations under Articles 7 and 10 of the Directive.

6.2 Directive 94/19/EC and the obligation of transposition

104. In its reply of 2 May 2011, Iceland submits that the Authority's claims in the letter of formal notice of 26 May 2010 are unfounded because Iceland had implemented Directive 94/19/EC correctly.[47]

105. Iceland appears to argue in the first place that it has fulfilled all its obligations by transposing the Directive 94/19/EC into its national law and by setting up a deposit guarantee scheme. It seems to claim that once the Directive has been transposed into national law, the state is exonerated from any further obligation under it.

106. The Authority disagrees. The Court of Justice has ruled consistently that a directive, by its nature, imposes an obligation on the states to achieve the result envisaged by it and all the authorities of the Member States must take all the appropriate measures, whether general or particular, to ensure fulfilment of that obligation.[48] The obligations under the EEA Agreement do not stop at transposition into national law.

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[46] Report of SIC, Chapter 17, pp. 123 and 124.
[47] Reply from Iceland to the Authority of 2 May 2011, pages 12-13.
[48] Case 14/83 *Von Colson and Kamann* [1984] ECR 1891, paragraph 26.

107. In the words of Advocate General Geelhoed:

> "The implementation process [...] is not concluded with the correct transposition of the provisions of the directive and the establishment of the organisational framework for the application of these provisions, it must also be ensured that these two aspects operate in such a way as to achieve in practice the result sought by the directive"[...]
>
> Beyond the 'paper wall' erected in the transposition phase, the Member States, [...] are and remain responsible for ensuring that the directive is applied and enforced correctly, in short, that its useful effect is achieved."[49]

108. Indeed, the Court of Justice has held consistently that:

> "the adoption of national measures correctly implementing a directive does not exhaust the effects of the directive. Member States remain bound actually to ensure full application of the directive even after the adoption of those measures"[50].

109. In addition, the objective of the Directive to enhance depositor protection would be compromised if the Directive were interpreted as only obliging Member States to set up a deposit guarantee scheme without any obligation to actually ensure that the aggrieved depositors are provided with compensation. Such an interpretation would also compromise the uniformity within the EEA of the minimum protection of depositors.[51]

110. The Court of Justice has consistently held that, where a provision of EU law is open to several interpretations, preference must be given to that interpretation

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[49] Opinion of Advocate General Geelhoed, Case C-494/01 *Commission v Ireland* [2005] ECR I-3338, paragraph 29.
[50] Case C-62/00 *Marks & Spencer* [2002] ECR I-6325, paragraph 27; see also Case C-494/01 *Commission v Ireland* [2005] ECR I-3331, paragraphs 116-117.
[51] See by analogy Case E-8/07 *Nguyen* [2008] EFTA Court Report p. 226, paragraph 27.

which ensures that the provision retains its effectiveness.[52] As stated above, the Authority considers that the provision in question is not open to differing interpretation. However, on the assumption that it would be, concluding that it entails an obligation of result is the only interpretation that retains its effectiveness, as otherwise the minimum protection envisaged by the Directive would be seriously jeopardised.

111. As a result, the argument of the Icelandic Government, according to which the simple setting up and recognition of a deposit guarantee scheme, irrespective of whether compensation of depositors is ensured under the conditions prescribed in the Directive, must be rejected.

112. The Icelandic Government also appears to argue that by adopting the "Emergency Law" and giving priority status to claims for deposits in the case of financial institutions becoming insolvent, Iceland fulfilled its obligations under the Directive.[53]

113. The Authority submits that such an adjustment to domestic bankruptcy law cannot be deemed to amount to compliance with Directive 94/19/EC. The very purpose of Directive 94/19/EC is to avoid depositors having to rely on bankruptcy proceedings and the associated hazards and delays, in order to receive the minimum amount of EUR 20 000. Simply facilitating the claims of depositors or of the Fund in bankruptcy proceedings does not constitute a satisfactory fulfilment of the obligation of result imposed by the Directive.

114. Secondly, Iceland seems to argue its own transposition was comparable to the manner in which other states have implemented Directive 94/19/EC. The Authority observes that such comparison is, as a matter of law, irrelevant with regard to whether Iceland has complied with its obligations under the Directive.[54]

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[52] Joined Cases C-402/07 and C-432/07 *Sturgeon and others* [2009] ECR I-10923, paragraph 47 and the cases cited therein. Also, judgment of the EFTA Court of 26 July 2011 in Case E-4/11 *Arnulf Clauder*, unpublished, at paragraph 48

[53] Reply of 2 May 2011 to the Letter of Formal Notice, pages 20-21.

[54] Case E-1/03 *The Authority v Iceland* [2003] EFTA Court Report p. 143, paragraph 33.

115. Moreover, the measures taken by Iceland were, in fact, not comparable to those of other States during the financial crisis that struck in the autumn of 2008. The other Member States took measures to avoid deposits becoming unavailable by recapitalising the banks. Moreover, no Member State made a distinction between domestic depositors and depositors in foreign branches. Thus, the depositors with the Icesave branches in the Netherlands and the United Kingdom are the only ones who have not received even the minimum compensation from the deposit guarantee scheme responsible under the Directive.

116. As noted by European Commissioner Michel Barnier in a letter to the Icelandic Minister of Finance Steingrímur J. Sigfússon (**Annex A 9 : Letter from Commissioner Michel Barnier to Minister of Finance Steingrímur J. Sigfússon dated 17 August 2010**):

> "as to the implementation of Directive 94/19/EC in the Member States of the European Union, we have no knowledge of any comparable situation in which depositors have not been compensated".[55]

117. Accordingly, Iceland's argument on the transposition of the Directive must be rejected.

6.3 Directive 94/19/EC and state responsibility

118. In its replies of 2 May 2011 and 30 September 2011, Iceland argues that the Directive does not require a state guarantee for the amount set out in Article 7 of the Directive and was never meant to place a financial obligation on the EEA States. Iceland even goes as far as implying that such a state guarantee would run against the Directive.[56] The Authority notes that, at the same time, the bill for the

[55] Published on the website of the Ministry of Finance.
[56] Reply from Iceland to the Authority of 2 May 2011, pages 20-21.

Budget Act 2011[57] refers to the Icelandic Government's declaration that deposits in Icelandic banks enjoy a state guarantee.

119. The Authority submits firstly that Iceland has mischaracterised the Authority's submission on this point. The Authority reproaches Iceland for failing to take any measures to ensure that depositors protected by the Fund receive the minimum amount guaranteed by the Directive. It appears clearly from the narration above that the Icelandic authorities themselves contemplated a number of different measures including the facilitation of a loan - as foreseen by Article 10 of Act no. 98/1999, or even the provision of a state guarantee to ensure payment of the minimum guaranteed within the time limit specified by Article 10 of the Directive. In practice, however, nothing was done. Iceland would seem to concede the argument on page 8 of its reply of 30 September 2011 that:

> "No government is liable or legally obligated to fund the system if such events [a complete collapse of the banking sector] unfold. The obligation is confined to taking measures to achieve a result, but does not translate into a funding result if the means are insufficient."

120. Quite so. The Authority's submission is simply that, as regards depositors in the foreign branches of Icesave, the Icelandic authorities in practice took no measures to achieve any result different from leaving those depositors without any guarantee at all.

121. In any event, the Directive cannot be interpreted as precluding the provision of a state guarantee should the Fund have inadequate resources to meet its minimum obligations.

122. In the Directive, the issue of state liability is addressed in the twenty-fourth recital of the preamble ("Recital 24"), which states that:

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[57] Section of the bill for the Budget Act 2011 concerning state guarantees. Also, the Memorandum of Understanding of 11 October 2008, referred to above, makes clear that the Icelandic State intended to guarantee the loan of the Dutch Government to the Icelandic Guarantee Fund.

> "this Directive may not result in the Member States' being made liable in respect of depositors if they have ensured that one or more schemes guaranteeing deposits or credit institutions themselves and ensuring the compensation or protection of depositors under the conditions prescribed in this Directive have been introduced and officially recognised" (underlining added).

123. This recital confirms that a Member State may be liable if it has not ensured that one or more schemes capable of ensuring the compensation or protection of depositors under the conditions prescribed by the directive, has been introduced.

124. Recital 24 cannot be interpreted as meaning that it limits the obligations of the Member States to simply setting up and recognising a deposit guarantee scheme in their territory, irrespective of whether the scheme is capable of ensuring the compensation or protection of depositors in accordance with the provisions of the Directive.

125. According to the wording of this recital itself it is not sufficient for Member States to set up and officially recognise a deposit guarantee scheme: merely doing so does not preclude any further liability in respect of depositors. Recital 24 is to be understood in the sense that further liability of the state is only excluded once depositors have been compensated or protected "*under the conditions prescribed in this Directive*". Recital 24 also makes clear that the depositors must be ensured compensation. If the obligation outlined above has not been achieved or cannot be achieved by the schemes established pursuant to the Directive, depositors are not compensated or protected "*under the conditions prescribed*" by it. Consequently, the exoneration of liability does not come into play.

126. This is confirmed by the statements of the Court of Justice in *Paul and others* in which the Court held:

> "[...] if the compensation of depositors is ensured in the event that their deposits are unavailable, as prescribed by Directive 94/19, Article 3(2) to (5) thereof does not confer on depositors a right to have the competent authorities take supervisory measures in their interest. That interpretation of Directive 94/19 is supported by the 24th recital in the preamble thereto, which states that the directive may not result in the Member States' or their competent authorities' being made liable in respect of depositors if they have ensured the compensation or protection of depositors under the conditions prescribed in the directive."[58]

127. The Court has thus clarified that if the compensation of deposits prescribed by Directive 94/19/EC is ensured, the state cannot be held further liable in damages for faulty banking supervision. It can be inferred from the judgment that if the compensation of depositors prescribed by the Directive is not ensured in the event that deposits become unavailable (which is the case in Iceland), the state should be held liable.

128. That does not mean that the Directive imposes on states an obligation to have in place a state guarantee absolving credit institutions from all responsibility for funding.

129. In its reply of 30 September 2011, Iceland relies on the Commission Staff Working Document of 12 July 2010, Document SEC(2010) 834 final,[59] to show that the Directive does not require a state guarantee. The passage quoted on page 7 of the reply of 30 September 2011 cannot be relied on to support such a conclusion. The passage is taken out of context. What the Commission describes on page 8 of the document is the scope of the impact assessment it carried out in support of the legislative proposal to amend Directive 94/19/EC. The Commission Staff Working Document does not examine whether Member States must put up a state guarantee for financing deposit guarantee funds.

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[58] Case C-222/02 *Paul and others*, cited above, paragraphs 30-31.

[59] Available publicly at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=SEC:2010:0834:FIN:EN:PDF

130. In its document, the Commission deals specifically and retrospectively with the cost of the increase in the guarantee coverage which had been brought about by Article 7 of Directive 2009/14/EC by the end of 2010. The Commission states that the cost of the increase was borne by banks. It also states that the recent crisis has shown that Member States choose an alternative to letting banks fail and then guaranteeing deposits through guarantee funds: the Member States support the banks directly. That direct support of the banks provides better security for the banking system and depositors than merely providing for payments through a deposit guarantee scheme. The Commission document states clearly – and correctly – that Member States do not have a legal obligation stemming from the Directive to step in and support the banks or even to prefinance the deposit guarantee fund. Footnote 11 on page 9 of the document simply concludes "… the increase in coverage level introduced by Directive 2009/14/EC would be viable even if governments were forced to repay depositors" because the recapitalisation measures were far more expensive than the increased deposit guarantee coverage proposed. The Commission document assumes that deposit guarantee schemes will be adequately financed to meet their obligations in practice: it does not envisage the peculiar situation in issue in these proceedings where a certain category of depositors are left without any protection whatsoever under the Directive.

131. Later on in its Staff Working Document of 12 July 2010, Document SEC(2010) 834 final, the Commission describes on page 19 how different deposit guarantee funds are financed. It states explicitly:

> "DGS [deposit guarantee funds] are principally funded by banks paying contributions to them. Currently, in 21 Member States such contributions are paid in advance on a regular basis (ex-ante) while in six Member States (AT, IT, LU, NL, SI and UK) banks only contribute after a failure (ex-post). Other financing sources are loans taken by the DGS or direct state interventions." (underlining added).

132. In any event, the Report of the SIC makes clear that the issue of a state guarantee was discussed at various points within the Icelandic administration should the Fund have inadequate monies to meet its legal obligations. No clear position was taken on this issue[60] even though the administration was aware at the relevant time of serious problems regarding the impecunious state of the Fund. [61]

133. But the States still have an obligation to achieve the result envisaged by the Directive and to take all the appropriate measures, whether general or particular, to ensure fulfilment of that obligation. That may mean, should all else fail, the state will ultimately be responsible for the compensation of depositors up to the amount provided for in Article 7, in order to discharge its duties under Directive 94/19/EC.

134. It is plainly a fact that the Icelandic State, either directly or through the Fund, has not ensured that the depositors in the Netherlands and the United Kingdom whose deposits were unavailable received any compensation from the Fund. Iceland is thus in breach of its obligations under the Directive.

6.4 Directive 94/19/EC and exceptional circumstances

135. In its replies of 2 May 2011 and of 30 September 2011, the Icelandic Government claims that the Directive does not apply in a financial crisis of the magnitude experienced in Iceland in the autumn of 2008, since no deposit guarantee scheme envisioned by the Directive could have dealt with such a systemic failure.

136. The Authority disagrees. The terms of the Directive itself cannot support such an argument. According to the case law of the Court of Justice, a Member State cannot plead exceptional circumstances to justify non-compliance with a directive in the absence of a specific legislative provision in the directive to that effect.

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[60] Report of the SIC, Chapter 17, p. 72. See also pp. 73 to 78.
[61] Report of the SIC, Chapter 17, p. 73.

137. In a case concerning pre-emptive rights under the Second Company Law Directive, Greece claimed, *inter alia*, that special measures were needed in order to avoid social disturbances. The Court of Justice noted that the Second Company Law Directive contained specific provisions for well-defined derogations and for procedures which may result in such derogations with the aim of safeguarding certain vital interests of the Member States which are liable to be affected in exceptional situations."[62] It continued:

> "It follows that, in the absence of a derogation provided for by Community law, Article 25(1) of the Second Directive must be interpreted as precluding the Member States from maintaining in force rules incompatible with the principle set forth in that article, even if those rules cover only exceptional situations. To recognize the existence of a general reservation covering exceptional situations, outside the specific conditions laid down in the provisions of the Treaty and the Second Directive, would, moreover, be liable to impair the binding nature and uniform application of Community law (see, to this effect, the judgment in Case 222/84 Johnston v Chief Constable of the Royal Ulster Constabulary [1986] ECR 1651, paragraph 26).
>
> As for the idea that rules comparable to those set out in Law No 1386/1983 might qualify under the derogation provided for in Article 41(1), it should be observed that that provision pursues a precise, well-defined social-policy aim, namely to encourage private individuals to hold shares. Like the exceptions provided for in Article 19(3) and Article 23(2) of the Second Directive, it is intended solely to encourage, in an objective and concrete manner, persons, such as employees, who generally do not have the means necessary to do so under the normal conditions of company law in the Member States, to participate in the capital of undertakings.

[62] Joined Cases C-19/90 and C-20/90 *Karella and Karellas*, [1991] ECR I-2691 paragraph 27.

Consequently, a national rule cannot take advantage of that derogation unless its practical application helps to achieve the objective of Article 41(1) of the Second Directive."[63] (underlining added)

138. Furthermore, the Court of Justice has held that the national authorities, including national courts, cannot, when assessing the exercise of a right conferred by a provision of EU law, alter the scope of that provision or compromise the objectives pursued by it.[64]

139. As stated above, no provision of Directive 94/19/EC itself exonerates the Member States from their obligations in exceptional circumstances such as a serious and general financial crisis.

140. Conversely, Directive 94/19/EC does envisage that exceptional circumstances may be present in a given case. However, such special circumstances may only, as an exception to the rule, justify delays in payment.

141. Under Article 10(2) of Directive 94/19/EC a guarantee scheme may, *in wholly exceptional circumstances and in special cases*, apply to the competent authorities for an extension of the time limit. Possible extensions are limited to a maximum of three months and cannot, in any event, be granted for longer than nine months in total.

142. The Icelandic authorities relied on this provision of the Directive when extending the deadline to 23 October 2009.

143. When adopting the Directive the legislator therefore made a conscious choice as regards the effect of possible exceptional circumstances. The effect of such circumstances was limited to allowing for an extension of the deadline to pay compensation but did not alter the obligation to do so.

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[63] Joined Cases C-19/90 and C-20/90 *Karella and Karellas*, [1991] ECR I-2691 paragraphs 31-33. See also, Case C-381/89 *Ekklissias v. Greek State*, [1992] I-2111, paragraphs 25 and 26.
[64] Case C-367/96 *Kefalas v. Greek State* [1998] ECR I-2843, paragraph 22.

144. Even with the experience of the financial crisis, the EU legislator has left the Directive largely unchanged, indeed strengthening it by increasing the coverage afforded to depositors and by reducing the payout time, and thus "*[maintaining] depositor confidence and [attaining] greater stability on the financial markets*".[65] Thus, Directive 94/19/EC has been, and will continue to be, an important stabilizing factor in times of exceptional circumstances such as a financial crisis.

145. Moreover, the Commission Staff Working Document lends no support to the idea that Directive 2009/14/EC cannot, as a matter of principle and because of the way different Funds are financed, apply in the event of a systemic banking crisis. The document states expressly on page 20:

> "It should be noted that the DGS Directive is applicable regardless of whether there is a systemic crisis or not. Otherwise it could not fulfil its objective to prevent bank runs. If DGS have insufficient funds, depositors may be paid out only after a very long delay or not paid out at all. If depositors are aware of this, they will lose confidence in DGS and may potentially run on their banks."

146. Accordingly, "exceptional circumstances" do not release the Icelandic Government from its responsibilities under Directive 94/19/EC and in particular from its obligation to ensure payments are made to depositors under Article 7(1) of that Directive.

147. Finally, Iceland argues that it was faced with an objective financial impossibility to comply with its obligations.

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[65] Recital 3 of Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay.

148. In that regard, the Court of Justice has consistently held that Member States may not plead financial difficulties to justify non-compliance with the obligation laid down in EU directives.[66]

149. It is only when there is a total physical impossibility, for reasons beyond all control of the EEA State, that the Court of Justice has accepted that a Member State is not in breach of its obligation under secondary law. The only example which could be found in the case-law related to an obligation to compile and submit data to the Commission, which could not be fulfilled because the data processing centre had been destroyed by a terrorist attack.[67]

150. However as ruled by the Court:

> "Although it is true that the bomb attack [...] may have constituted a case of force majeure and created insurmountable difficulties, its effect could only have lasted a certain time, namely the time which in fact would be necessary for an administration showing a normal degree of diligence to replace the equipment destroyed and to collect and prepare the data. The Italian Government cannot therefore rely on that event to justify its continuing failure to comply with its obligations years later."[68]

151. In the present case, while Iceland was faced with an unprecedented situation in October 2008, there was, as a matter of fact, no general declaration of unavailability of all deposits throughout the whole of the banking sector in Iceland. The Icelandic Government took measures to avert a general run on the banks in the domestic market and a general loss of access to domestic deposits.

152. Moreover, in any event, the breach as identified by the Authority in these proceedings has never been that Iceland was under an obligation to move all

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[66] Case 309/84 *Commission v Italy* [1986] ECR 599, paragraph 17; Case 42/89 *Commission v Belgium* [1990] ECR I-2821, paragraph 24 and Case C-375/02 *Commission v Italy* [2004] not published, paragraph 36-37.

[67] Case 101/84 *Commission v Italy* [1985] ECR 2629.

[68] Case 101/84 *Commission v Italy* [1985] ECR 2629, paragraph 16.

foreign deposits in full over to the new Landsbanki in October 2008. As a result of Iceland relying on Article 10(2) of the Directive, as it was entitled to, the obligation only ran out on 23 October 2009, a year after the crisis had unfolded.

153. At that time, the situation in Iceland was very different from the autumn of 2008 and the Icelandic Government cannot argue that it could not have had access to the funds necessary to fulfil its obligations under the Directive. This is evidenced by the conclusion, in June 2009, of an agreement with the Governments of the United Kingdom and the Netherlands, who were ready to provide the necessary funds to Iceland. Had this agreement been ratified, it would have allowed the Icelandic State to fulfil its obligations according to the Directive, within the time limits provided for in Article 10 of the Directive. Even though the terms might have been regarded as unfavourable, it is unquestionable that it was not impossible to gather the necessary funds to comply with the requirements of the Directive.

154. Finally, the Authority notes that today, three years after the deposits became unavailable, Iceland has still not paid the depositors in the United Kingdom and the Netherlands or their successors in title in accordance with the requirements of Directive 94/19/EC even though Iceland also seems to claim that the assets in liquidation are now sufficient to do so.

155. Thus, financial considerations related to the costs of complying with the obligations under Directive 94/19/EC cannot be invoked to evade the obligations under the Directive. Moreover, the facts of the case do not bear out that Iceland was faced with an absolute impossibility to comply with its obligations under the Directive.

EFTA SURVEILLANCE AUTHORITY

6.5 Non-discrimination

156. Iceland argues in its reply of 30 September 2011 that Article 4 EEA does not apply independently in this case because it applies only when no specific provision applies.

157. The Authority disagrees. When taking the emergency measures in response to the banking crisis in October 2008, the Icelandic Government made a distinction between depositors in domestic branches and depositors in foreign branches. As a result of the domestic deposits being moved over to the new banks, domestic depositors were covered in full, above and beyond the minimum required by Article 7(1) of Directive 94/19/EC, whereas the foreign depositors did not even enjoy that minimum guarantee.

158. By covering domestic deposits at least at the level prescribed by Directive 94/19/EC and within the time limits foreseen by the Directive, without providing foreign depositors with at least that minimum guarantee, Iceland has breached Directive 94/19/EC read in light of Article 4 EEA.

159. Indeed, the Court of Justice recalled in *Sturgeon* that "*[…] all Community acts must be interpreted in accordance with primary law as a whole, including the principle of equal treatment, which requires that comparable situations must not be treated differently […]*".[69]

160. Contrary to what is argued by the Icelandic Government[70], the ruling in *Sturgeon* is relevant for the interpretation of the EEA Agreement. The principle that all secondary legislation must be interpreted in accordance with primary law as a whole, including the principle of equal treatment, applies also in the EEA Agreement.[71]

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[69] Joined Cases C-402/07 and C-432/07 *Sturgeon and others*, cited above, paragraph 48.
[70] Letter from the Icelandic Government to the Authority dated 2 May 2011, page 24.
[71] Case E-3/02 *Paranova AS v Merck & Co., Inc. and Others* [2003] EFTA Ct. Rep. 101, paragraph 33.

161. As ruled by the EFTA Court, "the principle of homogeneity enshrined in the EEA Agreement leads to a presumption that provisions framed identically in the EEA Agreement and the EC Treaty are to be construed in the same way". It is only in specific circumstances that differences in the scope and purpose of the EEA Agreement as compared to the EU Treaties may lead to differences in the interpretation,[72] if the differences in scope and purpose constitute compelling grounds for such divergent interpretations.[73]

162. There are no grounds for allowing the EFTA States to disregard the principle of equal treatment when applying secondary legislation, a principle enshrined in both Article 4 EEA and Article 18 TFEU, using identical wording:

> "Within the scope of application of [this Agreement / the Treaties], and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited."

163. Directive 94/19/EC would therefore only allow the Icelandic Government to treat depositors with domestic branches differently from depositors at branches in other EEA States if they were regarded as not being in a comparable position. The Icelandic Government appears to acknowledge that position, as it is attempting to demonstrate that the two groups are not in a comparable position.

164. As a matter of law, both groups are in a comparable situation. Indeed, it follows from Article 4(1) of Directive 94/19/EC that all depositors with savings in branches, whether they are situated in the home state or in a host state, are in the same situation as regards the guarantee scheme set up pursuant to the Directive. This is made clear by the third recital to the Directive, which states that in the event of the closure of an insolvent credit institution, the depositors in any branches situated in a Member State other than that in which the credit institution has its head office must be protected by the same guarantee scheme as the

[72] Case E-3/98 *Rainford-Towning* [1998] EFTA Ct. Rep. 205, paragraph 21; Case E-2/06 *EFTA Surveillance Authority v The Kingdom of Norway* [2007] EFTA Ct. Rep. 164, paragraph 59.
[73] Joined Cases E-9/07 and E-10/07 *L'Oréal* [2008] EFTA Ct. Rep. 259, paragraph 31.

institution's other depositors. Therefore, in respect of the protection afforded by the Directive, it is clear that the two are in a comparable position.

165. By moving over the deposits of the domestic depositors only, thereby covering domestic deposits at least at the level prescribed by Directive 94/19/EC and within the time limits foreseen by the Directive, without providing foreign depositors with at least that minimum guarantee, Iceland has indirectly discriminated against foreign depositors on the basis of nationality, which is prohibited by Directive 94/19/EC read in the light of Article 4 EEA.

166. Indeed, the latter provision prohibits not only overt discrimination on the basis of nationality but also all covert forms of discrimination which, by the application of other distinguishing criteria, lead in fact to the same result. Such is the case for discrimination on the basis of residence[74]. And a distinction based on the location of the accounts amounts to a discrimination on the basis of residence.

167. In its replies, Iceland argues that it did not discriminate between depositors on the basis of residence, but on the basis of objective criteria which it lists.

168. Firstly, the Authority notes that most of the criteria allegedly distinguishing domestic and foreign depositors were not used as criteria by the Icelandic Government when it decided which depositors would be protected and which would not receive payment of even the minimum amount provided for in the Directive. This is the case, in particular, for the different denomination of deposits, the different overall relationship with the bank, the different availability of set-offs or the different connection to the Icelandic payment system.

169. Indeed, to the knowledge of the Authority, all depositors from the domestic branches of Landsbanki were carried over into the "new Landsbanki", even those with deposits in foreign currencies, who had no other business with Landsbanki,

[74] Case C-29/95 *Pastoors and Trans-Cap / Belgische Staat* [1997] ECR I-285, paragraphs 16-17; Case C-212/99 *Commission / Italy* [2001] ECR I-4923, paragraph 24.

who had no loans with Landsbanki and who did not have a special connection to the Icelandic payment system.[75]

170. Secondly, these criteria all favour residents and are essentially just another manner in which to distinguish between resident and non-resident depositors. For example, for the criteria relating to the different rates of return of accounts, the Icelandic Government is simply stating that it decided to discriminate between holders of accounts only available in Iceland and accounts only available in foreign branches. This is precisely what constitutes discrimination on the basis of residence, which is prohibited by Directive 94/19/EC and Article 4 EEA.

171. The Authority therefore does not alter its conclusion and considers that the holders of deposits in branches in Iceland and the holders of deposits in branches in other EEA States were, in their capacity as deposit holders in Icelandic banks, in a comparable situation as regards the protection granted to them by the Directive.

172. The purpose of the Directive being to improve consumer protection by ensuring minimum payment of compensation, nothing in the Directive suggests that any distinction may be made based on the location of the deposits and indeed such a distinction would run counter to the entire concept underlying the internal market. Consequently, it is a breach of the Directive to differentiate between depositors protected under the Directive by providing protection for some depositors while leaving others without any or any comparable protection.

173. The Icelandic Government then argues that even if its actions were discriminatory, they were justified by the need to restore the functioning and credibility of the domestic banking system and thereby Iceland's entire financial system. According to the Icelandic Government, it was necessary and proportionate not to transfer the non-domestic deposits because this would have

[75] See the FME's decision of 9 October 2008, points 7 and 8.

undermined the credibility of the rescue and stabilising efforts and made them meaningless.

174. The Authority cannot agree. Firstly, Directive 94/19/EC created a harmonised regime for the protection of depositors, thus depriving states from the possibility to justify rules which discriminate between depositors on the basis of residence in case of the deposits becoming unavailable. The Court of Justice has consistently held that a state cannot rely on any mandatory requirements as a reason for deviating from the harmonisation laid down in a directive in the absence of any express provision which permits the state to do so.[76] Iceland further argues that as Directive 94/19/EC effects minimum harmonisation, the caselaw relied upon by the Authority is inapplicable.[77] The Authority submits that it does not matter whether the harmonisation effected by a directive is full or minimum provided that the measures taken or omitted by the State fall within the harmonised field. If they do fall within the harmonised field, a State cannot rely on mandatory requirements to justify a breach of the directive in question. Clearly, in the present case, the failure by Iceland to ensure that the minimum compensation guaranteed by the Directive was paid out falls within the field harmonised by the Directive. As stated above, the Directive only allows exceptional circumstances to be relied upon to extend the deadline for payment of compensation.

175. Secondly, the present case does not concern whether Iceland was in breach of the prohibition of discrimination for not moving over the entirety of deposits of foreign Icesave depositors into "new Landsbanki", like it has done for domestic Landsbanki depositors. The breach is constituted by the failure of the Icelandic Government to ensure that Icesave depositors in the Netherlands and the United Kingdom receive payment of the *minimum amount of compensation provided for in the Directive* within the time limits laid down in the Directive, *like it did for the domestic depositors*. The compensation of domestic and foreign depositors above

[76] For example, Case 5/77 *Tedeschi* [1977] ECR 1555, paragraph 35, Case C-323/93 *Centre d'insémination de la Crespelle* [1994] ECR I-5077, paragraph 31.
[77] Reply of 30 September 2011 to the Reasoned Opinion.

and beyond that minimum amount has not and is not being discussed in the context of the present proceedings.[78]

176. In that context, the Icelandic Government cannot, as examined above, claim that it was impossible to comply with the requirements of the Directive without discriminating against non-domestic depositors. As indicated above, the Icelandic Government could have had access to the necessary funds, without jeopardizing the functioning of the domestic banking system and the real overall economy in Iceland.

177. This is evidenced by the conclusion, in June 2009, of an agreement with the Governments of the United Kingdom and the Netherlands, who were ready to provide the necessary funds to Iceland. Had this agreement been ratified, it would have allowed the Icelandic State to fulfil its obligations according to the Directive, within the time limits provided for in Article 10 of the Directive.

178. This is not to say that getting access to the funds could not have entailed high costs for Iceland. But it is settled case law of the Court of Justice and the EFTA Court that mere economic grounds cannot serve as justification for restrictions to the fundamental freedoms.[79] Iceland now argues that that settled caselaw does not apply in the present case given the magnitude of the financial crisis. It claims that its actions were justified for "the maintenance of the overall economy, society's institutions, essential public services, public policy and public security"[80] and refers to the judgment of the Court of Justice in Case 72/83 *Campus Oil*.[81] Iceland fails to indicate why the basic fabric of Icelandic institutions and public life and security could only be preserved by leaving foreign depositors in Icesave branches without the minimum protection required by the Directive. Iceland seeks comfort from the correspondence and Decision of the Authority mentioned

[78] In that regard, the Authority must stress that this does not prejudge its view as to whether the discrimination relating to the compensation of depositors above and beyond the level foreseen by the Directive is justifiable.
[79] See, *e.g.* Case C-367/98, *Commission v Portugal* [2002] ECR I-4731, paragraph 52 and the cases cited therein; Case E-1/04 *Fokus Bank*, cited above, paragraph 33 and Case E-1/09 *The Authority v Liechtenstein*, not yet reported, paragraph 36.
[80] Reply from Iceland to the Authority of 30 September 2011, p. 12.
[81] [1984] ECR 2727.

in footnote 6 on page 10 of the Reply of 30 September 2011 to the Reasoned Opinion. Suffice it to say that the correspondence and the Decision mentioned concern a complaint lodged by commercial creditors of the Icelandic banks and deal with a very different set of measures adopted by Iceland because they concern mainly the Emergency Act adopted on 6 October 2008 and the administrative decision adopted pursuant to it.

179. Finally, the Authority fails to understand how Iceland can simultaneously argue that it was financially impossible to comply with the Directive and refer to the fact that the recovery rate of at least 90% from the bankruptcy estate of Landsbanki "*is an important aspect in considering the Icesave issue*".[82]

180. Accordingly, the Authority takes the view that the Icelandic Government cannot advance any viable justification for the discriminatory measures taken against the foreign deposits in the circumstances of this case.

181. For the sake of completeness, the Authority notes that the fact that the United Kingdom and Dutch authorities have compensated the majority of deposit holders under their respective national deposit guarantee schemes is irrelevant with regard to whether Iceland has complied with its obligations under the Directive. The issue is how Iceland has treated different groups of depositors, not whether as a matter of fact they might be better or worse off.

182. It follows from the above that even if the provisions of Directive 94/19/EC were interpreted, contrary to the reasoning set out above, as not imposing obligations of result, by treating deposits located in Icelandic branches differently from deposits located in other EEA States, Iceland is in breach of Articles 4(1) and 7(1) of the Directive and/or Article 4 EEA.

183. Moreover, to the extent this differentiation in treatment of depositors protected by the Directive is not considered a breach of that Directive, it constitutes

[82] Reply from Iceland to the Authority of 2 May 2011, p. 10, also Reply from Iceland to the Authority of 30 September 2011, pp. 3 to 6 and pp. 12 and 13.

discrimination on the basis of residency prohibited by Article 4 of the EEA Agreement.

184. The Icelandic Government invokes in its reply of 2 May 2011 the reasons mentioned above to explain why there is no discrimination under Article 4 EEA and, in the alternative, why the discrimination can be justified. It contends that the assessment of discrimination on grounds of nationality is the same under Articles 4(1) and 7(1) of Directive 94/19/EC, on the one hand, and Article 4 EEA on the other. The Authority agrees. Therefore, these reasons the Icelandic Government has invoked as regards Article 4 EEA must be dismissed on the same grounds as for Directive 94/19/EC.

185. Accordingly, Iceland has failed to fulfil its obligations arising under Articles 3(1), 4(1), 7(1) and 10(1) of Directive 94/19/EC and/or Article 4 of the EEA Agreement by failing to ensure payment of compensation of 20 000 EUR to depositors on the so-called Icesave accounts of Landsbanki within the time limits laid down in the Directive.

7 Conclusion

186. Accordingly, the Authority requests the Court to:

a) Declare that by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and in the United Kingdom provided for in Article 7(1) of the Act referred to at point 19a of Annex IX to the Agreement on the European Economic Area (*Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes*) within the time limits laid down in Article 10 of the Act, Iceland has failed to comply with the obligations resulting from that Act, in particular its Articles 3, 4, 7 and 10, and/or Article 4 of the Agreement on the European Economic Area,

b) Order Iceland to bear the costs.

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Agents for the EFTA Surveillance Authority

List of Annexes

Annex	Designation	Cited at
Annex A 1	Chapter 17 of the SIC Report	p. 7 ¶18; p. 9 ¶24, ¶25; p. 10 ¶27; p. 11 ¶28, ¶29, ¶31; p. 12 ¶33; p. 13 ¶34; p. 32 ¶99, ¶100, ¶101; p. 41 ¶132
Annex A 2	Chapter 18 of the SIC Report	p. 7 ¶18; p. 8 ¶21; p. 9 ¶23; p. 13 ¶35
Annex A 3	Letter of Formal Notice of 26 May 2010	p. 18 ¶53; p. 24 ¶71
Annex A 4	Reply from Iceland of 2 May 2011	p. 19¶58; p. 26 ¶80; p. 27 ¶82; p. 28 ¶88; p. 33 ¶104; p. 35 ¶112; p. 36 ¶118; p. 47 ¶160; p. 49 ¶167; p. 53 ¶179; p. 54 ¶184
Annex A 5	Reasoned Opinion of 10 June 2011	p. 21 ¶60; p. 24 ¶71
Annex A 6	Reply of 30 September 2011 to the reasoned opinion	p. 15 ¶45; p. 21 ¶62; p. 26 ¶80; p. 37 ¶119; p. 39 ¶129; p. 49 ¶167; p. 51 ¶174; p. 52 ¶178; p. 53 ¶179
Annex A 7	Letter from Iceland of 13 December 2011	p. 22 ¶66; p. 23 ¶69; p. 30 ¶95
Annex A 8	Opinion of an expert group of 7 November 2008	p. 25 ¶76
Annex A 9	Letter from Commissioner Michel Barnier to Minister of Finance Steingrímur J. Sigfússon dated 17 August 2010	p. 36 ¶116