The Icesave Dispute in the Aftermath of the Icelandic Financial Crisis: Revisiting the Principles of State Liability, Prohibition of State Aid and Non-discrimination in European Law

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This study focuses on the Icesave dispute and Icesave agreements between Iceland, the UK and The Netherlands in the light of European law (EU and EEA law) and explores two main issues: 1) the State liability for breaches of EU/EEA law on the basis of Directive 94/19/EC following a systemic bank collapse in Iceland; and 2) the principle of non-discriminatory interplay between the nationalisation of Icelandic banks (State aid) and the payment of the minimum guarantee of €20.887 to depositors of Icesave accounts in the branches of Landsbanki in the UK and The Netherlands. This dispute was handled through diplomatic negotiations. The author is highly critical of the methodology followed. This cross-border dispute brought to light new complex problems in a grey area of European law which should have been brought before the highest European courts. Icesave also seems to have turned Icelanders against the process of European integration and the EU.

I. Introduction

Icesave has been one of the most difficult disputes that Iceland has faced since the end of the Second World War, and it has already marked the legal and political history of the country. This study will argue that while the Icesave dispute relates to a highly complicated problem created by the internal market of banking and financial services, the nationalisation of banking entities after a financial crisis presents a new challenge for EU law for which the EU Treaties and European jurisprudence had no legal answer during the 2008–2009 crisis.

Icesave raised important questions of European law (EU/EEA law) which were grey areas to be resolved in this field. As EU law is a dynamic field it is important to take into account the legal framework in which the events took place, rather than the legislation which may have been adopted later (principle of legality oblige). In the first place, the rules of State liability of EU/EEA law in this case were unclear and uncertain, due to the systemic crisis context and the lack of comparative data regarding implementation of European law in other countries. In the second place, it is questionable whether the Icelandic emergency measures violated EU/EEA law in the light of other national measures adopted by EU Member States during the crisis. In the third place, it is important to note that the alleged discrimination occurred on the basis of territory, not nationality. In the light of all this, it will be argued that the real core of the dispute is in fact the sovereign economic power of a country to re-organise its economy and financial system. The key issue is to determine whether European law obliged EU/EEA Member States at that time to nationalise private debt left by the collapse of the banks in the UK and The Netherlands without a connection to the Icelandic economy and territory. (The EU has no power of this kind because Member States hold all competence over their budget and tax systems.) Whether or not this obligation fell under the scope of EU/EEA law is a subject of interpretation and political will. If the EU/EEA has no power, the

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principles of State liability and non-discrimination in EU/EEA law do not come into play. In short, this study explores the scope, limits and tension between the effectiveness of European law and the sovereign economic independence of a nation defined by its territorial limits and human resources.

From a legal point of view it is highly relevant to note that this dispute has been approached so far outside the legal order and by diplomatic negotiations. Due to the specificities of EEA law, unless the three countries so agreed, Iceland could not take the case directly before the ECJ, and the EFTA Court had no direct competence either. In this context, one may wonder whether the structure of the EEA Agreement between the EU and EFTA countries proved inadequate for resolving a cross-border dispute of this magnitude. By approaching this dispute on a political basis, Icelandic and other European citizens residing in Iceland were deprived of access to justice as well as the Icelandic State. In spite of the importance of this dispute for the internal market and for all parties involved, the current methodology used meant that no right to effective judicial remedy existed for Iceland or Icelanders at European level, neither was there any judicial forum where all pleadings could take place and where the rule of law could prevail on the basis of legal arguments. A choice was made in favour of diplomacy vs. adjudication. While it is difficult for adjudication to be successful without having convincing legal arguments, it is a fact that diplomatic conflict resolution relies on a good dose of pressure and thus imposition. For this reason, Icesave also represents conflict between power-based and rule-based approaches to international law.

This study is highly critical of this political approach to solving a legal dispute that will define the legal history of Europe and Iceland and, by extension, European integration. Here European obligations and European rights are linked together. From the perspective of European law, it is highly questionable whether EU States are able to request compliance with obligations from an EFTA/EEA State and its citizens without at the same time providing a proper system of judicial review with appropriate rights of defence. Because the Icesave dispute raises essential questions concerning the effectiveness of European law vs. fundamental rights, solidarity, democracy, economic sustainability and solidarity between nations, these questions should be clarified before the Court of Justice of the European Union or the EFTA Court. Furthermore, only a legal approach can guarantee that the interpretation of European law which makes Iceland assume sovereign liability for the payment of depositors in the UK and The Netherlands after a systemic bank collapse will apply to all countries which are likely to face similar circumstances in the future. While an ECJ ruling is a source of European law and has authority erga omnes, a diplomatic agreement between three countries outside the EU/EEA legal order does not produce legal effects for all 30 EEA countries.

II. Background of the Icesave dispute

An account of the different facts and background of the Icesave dispute is explained below by the group INDEFENCE in Iceland. It collected 62,119 signatures requesting the President of Iceland in December 2009 not to ratify a legislative act (Icesave 2) and to submit the second Icesave bill to a national referendum:

"The autumn of 2008 will long be remembered in Iceland. During the first days of October it became apparent that the three largest Icelandic banks were in grave danger of collapsing, due to insufficient liquidity. Collectively, these three privately owned companies accounted for about 85% of the Icelandic banking system. Among them was the Landsbanki bank, responsible for the high interest Icesave accounts that had become very successful in The Netherlands and the United Kingdom. On Monday October 6th the government reacted urgently by passing legislation enabling the Icelandic financial service authority (FSA) to effectively nationalize the banks if they were deemed to be on the brink of collapse. This was conceived as an emergency measure to guarantee national security and permit the government to maintain the financial infrastructure necessary to keep Icelandic society functioning through the impending crash."
On that same day, Icesave depositors in The Netherlands and the United Kingdom were unable to gain access to their funds, allegedly because of technical problems, but more likely because of liquidity problems of Landsbanki. On Tuesday October 7th the Icelandic government seized control of Landsbanki, which it deemed had gone beyond the point of no return. The next day the British government invoked the Anti-terrorism, Crime and Security Act of 2001 to freeze the assets of Landsbanki, the Central Bank of Iceland and the Government of Iceland in the United Kingdom. The aim of this draconian and unprecedented action was apparently to protect the interests of British Icesave depositors. The Dutch government took similar, but less stigmatizing, steps to freeze the assets of Landsbanki in The Netherlands. A few days later all three of the main Icelandic banks had collapsed. The terrorism stamp destroyed what little faith the outside world had in many Icelandic businesses and blocked off numerous economic lifelines, making it effectively impossible to transfer funds between Iceland and the outside world for several months."

In Europe, deposits of individuals in commercial banks are guaranteed by a private insurance fund under EU/EEA rules. When the crisis hit Iceland in September-October 2008, it became clear that the private Icelandic DGS (Tryggjafjárnagarður) could not meet all depositors’ claims as it was a serious case of systemic bank failure. In order to guarantee the functioning of the banking and financial services in Iceland, a series of measures was adopted, notably the Emergency Act 125/2008 under which the Icelandic Financial Supervision Authority took control, declared the bankruptcy of the old banks and moved the deposits in Iceland to new banks while giving secured priority in the bankruptcy proceedings to the deposits abroad. The methodology adopted by Iceland was soon criticised. A question arose whether a sovereign State was liable or not under European rules if the Icelandic Fund, which was under the obligation to provide a minimum guarantee of €20,887 per account, were not able to meet all depositor claims. It is important to remember that this was the first time in the history of the internal market that a cross-border bankruptcy/insolvency had created a large number of victims in other European countries. In the autumn of 2008, the British and Dutch governments announced that their own funding and insurance schemes would refund the depositors in their respective countries. This was done in order to avoid further expansion of the financial crisis to the European internal market, and also to guarantee financial stability. However, the British and Dutch governments immediately claimed that the Icelandic State was liable without respecting the original legal arguments raised by Iceland, the country where the final bill would have to be paid by taxpayers. The EU institutions appeared to support the British and Dutch interpretation.

In the midst of the most serious financial crisis that Iceland has experienced in recent history, the Icelandic government took the political decision to accept the claims from the UK and The Netherlands and promised to honour its European obligations. Negotiations resulted in three signed bilateral agreements (known as Icesave 1, Icesave 2 and Icesave 3). Icesave 1 was in force in Iceland but was not accepted by the UK or The Netherlands.4 Icesave 2 and 3 never came into force following rejection in national referenda.

The Icesave dispute and agreements reflect a conflict between EU/EEA/International law which is very complicated because it is entangled in political, economic and sociological factors.5 From a legal point, the negotiations between Iceland, The Netherlands and the UK concerning the Icesave deposits in the latter two countries refers to different legal issues in European Union law that can be summarised on two essential points: 1) the interpretation of Directive 94/9/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes (DGS) concerning the final responsibility/liability of the Icelandic Government as a last resort, and 2) the application of the principle of non-discrimination in EU/EEA law with regards to the Icelandic legal measures of nationalisation of Icelandic banks adopted after the financial crisis.

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4. Iceland, Bill amending Act No 96/2009 (Icesave 1). A second bill was passed on 30 December 2010 (Icesave 2). A third bill was passed on 16 February 2011 (Icesave 3).

5. The bilateral agreements (1, 2 and 3) were negotiated between Iceland, the UK and The Netherlands outside the European legal order (by means of diplomacy) but in the referenda held on 6 March 2010 and on 9 April 2011 they were perceived by 93% and 58.9% of Icelandic voters as negotiated under duress and jeopardizing the economic future of the small country.
III. Assessment of the legal claims in the context of European law (EU and EEA law)

The arguments for claiming a sovereign guarantee from Iceland for the compensation of depositors abroad are based, on the first place, on the interpretation of the law of the European Economic Area (EEA), taking into account its effectiveness in giving rights to individuals, and around two positions in particular:

1) that the Icelandic Government was obliged to assume responsibility and provide as a last resort the minimum guarantee of at least €20,887 for each Icesave depositor at Landsbanki in the UK/The Netherlands under Directive 94/19/EC, whether or not there was a financial collapse; and

2) that Iceland’s legal actions adopted by the Financial Services Authority in order to re-structure, recapitalise and create the new Landsbanki and the other Icelandic banks after the major crisis were discriminatory under EU/EEA law against depositors who were non-resident in Iceland.

The EFTA Surveillance Authority (ESA) in its Opinion of 26 May 2010 considered that the applicable Directive 94/19/EC introduces an obligation of result for the compensation of depositors in case deposits become unavailable which makes the State liable if this result is not achieved. In its view, this obligation is still applicable in the case of a major and general banking crisis so that exceptional circumstances do not release the State liability. This obligation is not reduced either if the amounts available in the fund are insufficient to cover all deposits. Last but not least, the ESA argued that by treating deposits located in Icelandic branches differently from deposits located in other EEA States, Iceland is in breach of the principle of non-discrimination. The European Commission, in a letter to the Icelandic Minister of Finance, declared that the Commission shared the legal analysis done by the ESA but left unanswered the question raised by the Icelandic Minister of Finance on how the alleged misimplementation of Directive 94/19/EC was defective in Iceland, considering the manner of implementation of the Directive in the other 27 EU Member States.

1. Background of EU and EEA structure and procedures for cross-border disputes

It is important to remember that the current European legal system is based on one European integrated internal market with two legal orders, the EFTA/EEA on one side, and the EU on the other. Two courts of justice are competent: the ECJ for the EU pillar, and the EFTA Court for the EEA pillar. Although there is a strong judicial dialogue between these two courts, the fact is that there is no direct judicial procedure designed to deal with cross-border legal issues occurring in the intersection of these two legal orders, as Icesave dispute shows. Problems of this kind need to be dealt with at political level or by indirect means through judicial interpretation.

The ECJ has exclusive competence to interpret EU law. The interpretation of the different EU/EEA institutions or EU Member States cannot be regarded as the final position. In some cases the ECJ also has jurisdiction in EFTA and EEA matters. The interpretation of EEA law belongs, in the last resort, to the ECJ when it affects the legal order of the EU (i.e. on issues relating to the Internal Market). However, the competence of the EFTA Court cannot be excluded if all parties to the dispute agree to take the dispute before it on the basis of the EEA Agreement and the EFTA Court Agreements, or if the EFTA Surveillance Authority (ESA) brings a case before the EFTA Court, or if any indirect action is exercised at national level (i.e. on request of an advisory opinion by a domestic judge in Iceland).
This figure illustrates the structure of the EEA Agreement. The left pillar shows the EFTA States and their institutions, while the right pillar shows the EU side. The joint EEA bodies are in the middle. Resolution of the disputes between EU and EFTA/EEA Member States belong to the highest political organ of the EEA, the EEA Joint Committee or the EEA Council. It was not until May 2010 that the ESA issued a legal opinion on Icesave opening up the possibility of a process of judicial adjudication before the EFTA Court.

2. Icesave dispute: Claim 1 – State liability under Directive 94/19/EC

The British and Dutch Governments claimed, in the first place, the State liability of Iceland under the Directive 94/19/EC (applicable in Iceland at the time of events). According to this Directive, Member States must guarantee that a deposit guarantee system (DGS) is in place. This guarantee is financed by obligatory contributions to a private fund existing in all EU/EEA countries. As the case Peter Paul and Others states, this "Directive 94/19/EC seeks to introduce cover for depositors, wherever deposits are located in the Community, in the event of the unavailability of deposits made with a credit institution which is a member of a deposit guarantee-scheme." In their view, depositors held by consumers were guaranteed in Europe up to the amount of €20,887 in all circumstances because otherwise the Directive would be of no use in practice. This claim was later supported by both the ESA and the European Commission in their legal analysis. The main problem of the Directive 94/19/EC is that in the event of a systemic failure of almost all banking institutions it does not specify the role of the State should the DGS fail to have sufficient funds. The obligation of Member States is to introduce a guarantee system; not to underwrite sovereign liability for the fund. All EU/EEA countries are obliged to adopt a law to make it obligatory for financial institutions to participate in a private fund to which credit institutions contribute. In principle, if the fund cannot meet depositors' claims in the event of a default by a member of the scheme, the remaining credit institutions have to make up the difference. In other words, the bankruptcy of a financial institution is covered - as in classic insurance systems - by the rest of the institutions active in the market. This was obviously impossible in the case of the Icelandic Fund (Tryggingsrjóður).
as the remaining Icelandic credit institutions which survived the crisis were far too small in relation to the claims of Icesave depositors in the UK and The Netherlands.

According to unofficial sources\(^\text{17}\) (as negotiations on the Icesave agreements have been kept secret from the public), the Icelandic government defended the immunity of the State at an early stage of discussions with the UK and The Netherlands and other EU countries. It claimed that the Directive had never been intended to cover up the case of a systemic failure, and that it did not impose a sovereign guarantee to make up for deposit insurance schemes. It might have repeatedly asked that the matter be taken to the EFTA Court, pointing to Recital 24 to the directive which says:

"Whereas this Directive may not result in the Member States' or their competent authorities' 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 recognized;"

Also during those negotiations, according to non-official sources, all the EU Member States contested the interpretation of the Icelandic government. They considered that a sovereign 'guarantee of last resort', similar to the role of central banks as 'lender of last resort', was the only way of "ensuring the compensation or protection of depositors." In their opinion, this was implicitly required by the Directive. Without this guarantee given by the State, it was argued against Iceland that European law would be deprived of its effectiveness as depositors would lose out in the banking institutions and the whole system would collapse.

It is difficult to deny that EU/EEA law was very unclear on this issue at the time of the events, this being one of the grey areas of European financial law. The ruling of the ECJ in the case \textit{Peter Paul and Others} previously mentioned\(^\text{18}\) was not sufficiently clear on this point to apply to the Icelandic case: While, on one hand, the ECJ requests that the minimum compensation be given to depositors (the minimum amount set by the Directive), the Court adds that there is no State liability for the German authorities for alleged failings in banking supervision (as per Recital 24). The interpretation of the provisions of Directive 94/19/EC in the event of systemic failure of a banking system – and in exceptional economic circumstances that bring a country to the brink of financial failure – is a very serious and problematic issue which had not been foreseen by either the European Directive or the Icelandic law. To sum up the problem, this Directive had never anticipated the event of complete banking failure in one country leaving depositors unprotected in another country (cross-border case of bankruptcy and insolvency).

On 25 November 2003, Advocate General Stix-Hackl delivered his opinion on the Peter Paul case explained in recital 117:

"As far as Community law is concerned, Directive 94/19 contains an exhaustive set of special provisions regulating deposit-guarantee schemes. It does not, however, exhaustively regulate the unavailability of deposits under Community law, only requiring the Member States to provide for a harmonised minimum level of deposit protection."\(^\text{19}\)

The European Directive gave no instructions regarding the discretion of the Member State if the private fund or DGS became insolvent because of the total collapse of a national banking system. The UK and The Netherlands requested from Iceland a State guarantee of last resort, a sort of State liability without a necessary breach of the State of its obligations under the Directive in the light of the events of 2008. But the paradox is that EU/EEA States cannot provide guarantees to their banking systems because this would fall under the prohibitions of European competition and State aid rules. If States did back up their private banking and financial institutions, all depositors in Europe would choose banks from larger Member States such as Germany and banks from small countries such as Luxembourg would not have a chance to compete. This goes against the basic principles of the internal market.

If the Directive 94/19/EC was silent on this point, it can be argued that the general doctrines of State liability for breaches of EU/EEA law applied. And, in this sense, State liability is not automatic in EU/EEA.

\(^{17}\) Various documents released on the Internet are available at \texttt{http://www.island.is} (last accessed on 21 July 2011).


\(^{19}\) Opinion given by Advocate General Stix-Hackl in the Case C-222/02 \textit{Peter Paul}, ECR (2004) I-09425 who argues that, even if the State liability was a necessary conclusion of the Directive 94/19/EC, the maximum responsibility for the State would be to compensate the depositors up to the minimum guarantee of €20,889.
law. This is the jurisprudence Francovich, Brasserie/ Factoriame in the EU legal order20 and Erla Maria, Karlsson and C. Nguyen in the EEA legal order21.

State liability for breaches of EU/EEA law is a doctrine of European law that is not found in the EU/ EEA Treaties but rather in the jurisprudence of the ECJ and the EFTA Court. In both legal orders the same conditions apply: 1) the rule of law infringed must be intended to confer rights on individuals; 2) the breach must be sufficiently serious; and 3) a direct causal link must be established between the breach of the obligation resting on the State and the damage sustained by the injured parties; on many occasions, the crucial element in this ‘multiple test’ will often be the clarity and precision of the rule breached.

It could be convincingly argued that Iceland had complied with its obligations under the Directive 94/19/EC because the State obligation ended once the Fund had been put into place. Nothing in the Directive 94/19/EC confirmed the responsibility of the State to supply funds through its general budget (nationalisation or bail-out financed by tax-payers) should the DGS or Insurance Fund (Tryggingsafóður) become insolvent. And this was precisely the Icelandic problem. With the Emergency Act, Iceland opted instead for giving depositors abroad a secured claim in the wind-up and resolution proceedings of Landsbanki – reimbursing depositors with the bank’s assets through bankruptcy law without nationalising the debt.

In May 2009, the EU revised Directive 2004/19/EC and a new Directive 2009/19/EC was adopted.22 The issue of the State guarantees and State liability was still unclear and undefined. Nowhere in the text could the terms ‘immunity’ or ‘liability’ be found. The so-called principle of the State liability when a systemic failure provoked the lack of funds in the private DGS to cover all depositors was, once again, not directly regulated.

The only recital related to this issue was recital (13) which states that:

“Member States should aim at ensuring the continuity of banking services and access to liquidity of banks, in particular in periods of financial turmoil. For this purpose, Member States are encouraged to make arrangements as soon as possible for ensuring emergency payouts of appropriate amounts upon the application of the affected depositor, within no more than three days of such application. Since the reduction of the current payout delay of three months will have a positive impact on depositor confidence and the proper functioning of the financial markets, Member States and their deposit-guarantee schemes should ensure that the payout delay is as short as possible.”

The new Directive 2009/19/EC still left unclear the issue of liability/immunity of the Member States as a last resort. What is meant by emergency payouts? Are tax payers obliged to pay for the deposits when the private insurance scheme funds are insufficient? It seems an unfair demand and paradox to request under EEA law that Iceland follow this interpretation while at the time of the events the EU Member States were not able to agree on this principle for the EU pillar.23

In practice, while the European legislator left the issue unclear for competition and State-aid reasons, this meant that the ECJ would have had to rule on the problem. However, while the principle of homogeneity requires comparable rights and obligations under EU and EEA law, the diplomatic approach followed meant that Iceland did not have a chance to request a proper interpretation of EU/EEA law before this European court.

Other articles and papers from scholars and other institutions pointed out the weakness of the European rules on Deposit Guarantee Schemes at that time and the insufficiencies of the rule of the home country control in the event of systemic failure of

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21 State liability for breaches of EEA law is a doctrine created by the EFTA Court; see Cases E-7/97 Erla Maria Sveinbjörnsdottir v. 1998 EFTA Court Report, 93; Case E-4/01 Karl K. Karlsson M. v. The Icelandic State, 2002 EFTA Court Report, 249; Case E-1/07 Criminal proceedings against A, 2007 EFTA Court Report, 245; and Case E-8/07 between Celina Nguyen and The Norwegian State, Judgment of 20 June 2008, not yet published in EFTA Court Reports, see OJ C 33, 7.2.2008, p. 10.


the banking system in one country due to the interdependence of the financial markets and the lack of a single overarching European supervisor or regulator and the lack of coordination between national authorities.\textsuperscript{24} I will come back to this argument later.

To conclude this section the following can be said. It can be argued that the State liability for Iceland for breach of EEA law in the Icesave dispute is very unclear, a point that has been agreed by many legal experts in European law\textsuperscript{25} and can be argued in both affirmative and negative senses. Directive 94/19/EC did not require it. Directive 2009/19/EC is silent on this issue and the jurisprudence of the ECJ was not sufficiently clear for the resolution of this case due to a new context. Providing State guarantees for private banks would violate EU competition and State aid rules. And, even if the European legislator decided to adopt this principle in 2011, it would still not be possible to apply it to the events that took place in 2008 (principle of legality).

As the issue of the liability/immunity of the State in the case of a systemic bank failure at that time is imprecise, as well as the role of the host/home States involved in the dispute and financial supervisory authorities should have been discussed in much greater detail regarding obligatory consumer protection and financial stability requirements, and as it was advisable to clarify the ECJ jurisprudence \textit{Peteer Paul and others} from the ECJ in 2004,\textsuperscript{26} one may conclude that it should have been the role of the ECJ or the EFTA Court to provide an interpretation of the relevant EU/EEA law, given that European law was not clear enough (doctrine CILFIT).

3. Icesave dispute: Claim 2 – Principle of non-discrimination in connection with the re-structuring of the Icelandic financial system (State aid)

The second claim of the British and Dutch governments is that Iceland was in breach of its obligations under Article 4 of the EEA Agreement which prohibits "any discrimination on grounds of nationality", echoing the new Article 13 of the Treaty on the Functioning of the European Union (TFEU) (ex Article 7 EC Treaty).\textsuperscript{27} The ESA legal opinion of May 2010 and the European Commission supported this claim.\textsuperscript{28}

One more, according to unofficial sources,\textsuperscript{29} it seemed that Iceland had tried to contend that its policy was "based on objective considerations independent of the nationality of the persons concerned" (the consideration being the location of the branches of the collapsed banks) and that it was "proportionate to the objective being legitimately pursued" (the legitimate objective being the survival of the whole banking system in Iceland in a situation of extreme financial distress and economic crisis).\textsuperscript{30} Even today, Iceland has not guaranteed deposits in Iceland by law if the current insurance fund were to become insolvent again.\textsuperscript{31} The only guarantee is a political statement made by the Prime Minister in autumn 2008. What is more, Iceland would have argued that there has been no discrimination based on nationality as both Icelanders and other Europeans had benefited from the nationalisation measures adopted by the emergency measures (deposits in Iceland were continued), and both Icelanders and other Europeans with deposits in overseas branches were negatively...


\textsuperscript{25} Articles published by Professor Stefan Máir Stefánsson on Icesave in the Icelandic newspaper Morgunblaðið on the 12, 13, 14 and 15 January 2010; see also Report by law firm Milácnin de Reyes to the Icelandic Parliament 19 December 2009, not published, on the second Icesave agreements negotiated between Iceland, the UK and The Netherlands. Report available on the Internet at \textless www.island.is> \textless www.independence.is> (last accessed on 21 July 2011); see also interview with MEPs Eva Joly and Alain Lieplz ınt Iceland, programme Síllar Egis, broadcasted on 10 January 2010.

\textsuperscript{26} ECJ, Case C-222/02 \textit{Peter Paul v. Bundesrepublik Deutschland} (2004) ECR 1-09425.

\textsuperscript{27} For a national court of last instance there is an obligation to refer to the ECJ if EU law is not sufficiently clear. In order not to refer to, the matter must be equally obvious to other national courts. ECJ, Case 283/81 \textit{Cilià sr v. Ministro della Sanità} (1982) ECR 3415.

\textsuperscript{28} The UK and The Netherlands argue that, by placing all deposits located in Iceland at new Icelandic banks, covering all Icelandic institutions but letting overseas branches go insolvent, the Icelandic government was unfairly (or "illegally") guaranteeing the deposits for Icelandic residents or residents in Iceland, individuals or corporations, and therefore discriminating deposits in the UK and The Netherlands on the basis of nationality.

\textsuperscript{29} EFTA Surveillance Authority, Letter of formal notice to Iceland, supra note 6, and Letter of Michel Barnier, European Commissioner, supra note 7.

\textsuperscript{30} All documents are available on the Internet at \textless www.island.is> and \textless www.independence.is>.

\textsuperscript{31} The situation is complicated by the position of the different treatment of the so-called "wholesale" deposits in Iceland by comparison to the UK and the Netherlands.

\textsuperscript{32} Articles published by Professor Stefán Máir Stefánsson in Morgunblaðið, supra note 25.
affected by the controlled winding-up of the financial institutions. Iceland, furthermore, justified the different situations between domestic and foreign depositors. While deposits in Iceland transferred to the new banks were to remain in the country due to the strict currency exchange restrictions introduced by the Emergency Act, deposits abroad would not have remained within the Icelandic financial/economic system. Depositors were not in comparable situations. The economic and financial future of the country was at stake.

As in the previous case, according to non-official sources, the UK, The Netherlands and the rest of the EU countries would have rejected the Icelandic arguments and would have argued for a case of indirect discrimination “de facto” based on nationality.

EU law and ECJ jurisprudence are very strict on the principle of non-discrimination. This principle applies to all areas of EU law, including the free movement of capital and payments34 and competition and State aid.35 The most relevant provision of primary EU law is now Article 18 Treaty on the Functioning of the European Union (TFEU) (ex Article 12 TEC) the principle of non-discrimination on grounds of nationality.35 On the other hand, EU law also admits that Member States can justify State aid on the basis of “serious disturbances in their economies”. Exceptional circumstances would justify exceptional measures.36

As stated above, the principle of discrimination was developed by the jurisprudence of the ECJ and the EFTA Court. The EU Treaty and the EEA Agreement both allow exceptional derogations to the internal market rules; however, they fall under close judicial scrutiny and must respect the non-discrimination principle.37 According to EU law, any national rule, discriminatory or non-discriminatory, which affects the internal market and free movement of goods, persons, services or capital to another Member States market, falls under EU Law and must be justified. In this sense, national measures liable to hinder/afford the internal market must pass a strict test.38 In the absence of a legal definition, the Court of Justice defines discrimination and inequality as arising from the application of different rules to comparable situations or the application of the same rule to different situations.39 The main problem with this argument is that it refers to discrimination on grounds of nationality, while discrimination on grounds of territory is not considered in EU law for obvious reasons of sovereignty and generally due to the lack of extraterritorial scope of national laws and national powers.

The essential question that European law must still answer is the following: is discrimation on the grounds of territory also prohibited by European law when in its effect it amounts to a discrimination based on nationality? And then, other questions arise which are no less important: Does the State restricting of the Icelandic banks in an emergency situation that creates new entities with all deposits within the Icelandic territory (held by not only Icelandic but also European citizens) and gives secured priority in bankruptcy proceedings for depositors of the branches of Icelandic banks in The Netherlands and the UK, constitute a violation of the EU legal principle of discrimination on the grounds of nationality? Are depositors abroad and domestic depositors in comparable situations when public tax money has to be used for the financial rescue of the country?

Too many reasonable doubts still persist, even after careful consideration of different available sources: general EU law; the policy and legal analysis followed by both EU and EEA institutions during the financial crisis such as the Opinion of the EFTA Surveillance Authority on the legality of the Icelandic Emergency Law under the EEA Agreement;40 the Report issued by the European Central Bank (ECB) on the national rescue measures adopted by all different 27 EU countries;41 the opinion of the Commi-

33 Art. 63 (ex Art. 56 TEC) and 65 TFEU (ex Art. 58 TEC).
34 Art. 107 TFEU (ex Art. 87 TEC).
35 This article reads: “Within the scope of application of the Treaties, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited”.
36 And this is precisely the argument used by the European Commission to justify general guarantees given by different EU States to depositors in their territory during the financial crisis in 2008–2009. European Commissioner Neelie Kroes, speech given in Brussels on 6 October 2008, available on the Internet at cwww.europa.eu> (last accessed on 21 July 2011).
38 Craig and De Bórcas, EU Law, supra note 37.
40 EFTA Surveillance Authority, of 4 December 2009, available on the Internet at chttp://www.esfa.int/> (last accessed on 21 July 2011).
sion on the case of Ireland in October 2008; the opinions of the ESA of May 2010 and the letter from the European Commission from August 2010, and also other arguments developed by Professor Stefán Márd and lawyer Larus Blöndal in the Icelandic press. It is possible to argue that the interplay of the principle of non-discrimination and the rules of State aid for nationalised banks in a post-bankruptcy situation is not clear in European law. Is the non-discrimination principle test developed by the ECJ for nationality also applicable to territory? Have other countries respected the principle of non-discrimination by reason of nationality and/or territory while adopting national rescue measures for banks during or after the financial crisis?

Once again, it would be possible to put forward different arguments, depending on whether emphasis is put on 1) the effectiveness of European law (obligation of result) and the rights of depositors to recover the minimum guarantee in all circumstances, or on 2) the fact that discrimination on grounds of territory is not prohibited by EU/EEA law, hence the dispute affects the core of the sovereign power of a country (taxation power and national budget) and so stays outside the scope of EU/EEA law, and, last but not least, 3) the fact that depositors outside the country are not in a comparable situation to depositors resident in the country when the national budget has to be allocated.

It is true that Iceland is the only country to have experienced a complete collapse of its banking system. National measures were adopted and the banks were nationalised and recapitalised and are now under a process of controlled winding-up and liquidation. Domestic deposits have been re-established and foreign deposits given priority in bankruptcy proceedings. The use of taxpayers' money to recapitalise or nationalise banks and financial institutions and assure a financial market finds a natural limit in the territorial limits of a country. From this perspective, it is totally legitimate to question whether EU and EEA laws cover this tragic problem for depositors located in Europe and whether the principle of non-discrimination by reason of territory must prevail over a sovereign debt that jeopardises the whole economic sustainability of a country with a small population.

Several arguments prove that the interpretation supported by the UK, the Netherlands, the ESA and the European Commission was far from clear and might even have been biased. In the first place, the financial crisis revealed that governments had acted under national law. There was no EU legal basis for managing crises in the banking sector. The EU persistently maintained a position of supporting intergovernmental coordination. Although there was some common action plan and guidelines adopted at European level, the EU institutions, including the ECB, still have no role in the adoption of national measures (known as bail-out) designed to nationalise domestic banks operating within the territories of the Member States. The last word belongs to national authorities because there is no single European treasury.

In the second place, the EU has insisted that the Icesave dispute and agreements should be dealt with bilaterally between Iceland, the UK and the Netherlands. The dispute was approached via diplomatic negotiations and international agreements. The EU claimed no competence or powers in this regard. Icesave has clearly shown that the lack of an EU regime hampers the ability of governments to deal with problems in cross-border situations.

In the third place, it must be acknowledged that although the European Commission has repeatedly said that all national measures adopted should be required to take account of their effects in the other EU countries and that the principle of non-discrimination should be respected, the truth is that the following essential terms ‘State liability’, ‘discrimination’, ‘equality’ do not appear anywhere in the Report published by the ECB in July 2009.
which evaluates the legislation adopted in different 27 countries.48

In the fourth place, the case of Ireland is a good example of the thinking of EU institutions at that time. According to the publication of Commission Communication on State aid guidelines from 13 October 2008, Governments had to ensure that every bank active on their territory would gain access to the rescue measures, regardless of nationality. This was one of the main arguments raised by the Commission against Ireland’s rescue plan presented in autumn 2008. The European Commission asked Ireland that all banks incorporated or operating in the country had to be covered by the national rescue measures.49 But, as the Commission explained, the non-discriminatory principle had to guide the action of the Irish government towards all banks with systemic relevance to the Irish economy, regardless of origin. This principle of non-discrimination does not come into play when banks are not related to the economy of Ireland.

In the fifth place, it is questionable whether a country of 318,000 citizens such as Iceland can rescue the savings of over 400,000 depositors abroad without jeopardizing its own economic future. And, even if it could do so, it is questionable whether such a request was legitimate in the light of the European integration and EU/EEA legal orders. Are there any limits to the effectiveness of European law? The scope of EU/EEA law cannot be extended “ad hoc” by EU countries or EU/EEA institutions if the interpretation affects the budgetary powers and the economic sovereignty of a country.

In view of the above considerations we end this section as follows. Because the state liability derived from Directive 94/19/EC was unclear for the Icelandic case (systemic bank collapse), and because the national rescue measures adopted by some EU Member States need further research concerning the respect of the principle of non-discrimination on grounds of territory, it is extremely important to clarify the competences of the EU regarding the real core of this dispute: the existence or not of powers regarding national rescue measures in response to the financial crisis and the nationalisation of banks and debt created by private entities.

4. On the competences of the EU regarding nationalisation of banks in emergency circumstances

The EU insisted that this was a bilateral dispute during 2009 until August 2010, and the ESA did not take action until May 2010. These two factors bring into question the competence of the EU/EEA institutions and the whole validity of legal arguments maintained by the UK and the Netherlands. Was Iceland really only a bilateral dispute? This author argued during 2009 that consistency was needed. If indeed it was the case that the EU/EEA did not have the competence to deal with this dispute, this was because the real issue under discussion fell outside the scope of European law.

Only if the competences had been transferred to European level would the principle of discrimination on grounds of nationality apply in EU law. Extending the scope of the discrimination principle from nationality basis to territorial basis is a serious issue. And, even in this case, another question mark might rise in the framework of EEA law because it is not automatic that all EU law is incorporated into the EEA legal order as EEA law does not have the same wide material scope as that of the EU which has accumulated over the years.50

It is important to remember that nothing in either the new Treaty of the European Union or in secondary law at that time made provisions for a role or competence to be given to the EU to deal with national measures designed to nationalise, bail-out or restructure domestic banks in emergency situations such as the 2008 financial crisis requested during critical moments.51 Furthermore, taxation and

48 Ana Petrovic and Ralph Tutsch, National Rescue Measures In Response To The Current Financial Crisis, supra note 41. It is also very unclear from this Report whether nationalisations measures adopted to be adopted by Austria, Germany, Ireland, Latvia, Lithuania, Poland, Portugal and the UK in 2009 would pass the same non-discrimination test that Iceland has been imposed to accept by diplomatic means.


50 M. Elvira Méndez-Pinedo, EC and EEA law, supra note 8.

economic national policies are so closely linked to national sovereignty that they are considered as extremely sensitive areas within the European integration project.

It could be convincingly argued in European law that the nationalisation of private debt in emergency circumstances created by the collapse of practically the whole banking system of a country does indeed fall outside the scope of EEA law.52

It is undeniable that this whole affair is a very delicate problem created by the internal market and it is unfortunate that it has affected depositors in other EU countries. The truth is there was no explicit EU competence to act available in the EU Treaties. If the problem falls outside the scope of the EU Treaty, the competence belongs to the Member States and countries have the sovereign right to decide whether or not they will nationalise insolvent banks or branches operating in other territories. As the European Commission recognised in the Irish case, the link to the nation’s economy would be the essential guiding light. A revision of the different legislations adopted by different EU countries as stated in the Report of the ECB, which had adopted nationalisation provisions, confirms that the EU has no direct nor explicit competences when emergency circumstances are so extreme.

It is very important to note that internal taxation and budget allocations are highly sensitive areas that fall under the competence of EU Member States. The debt claimed by the UK and the Netherlands amounted to €8,900,000 per Icelandic family not counting the interest. The democratic principle “no taxation without representation” applies. Even after the entry into force of the Lisbon Treaty, national vetoes remain on taxation and social security issues. Fiscal sovereignty remains at national level53 while Member States must ensure that it complies with the main principles of EU law. Tax policy is a symbolic and important element of national sovereignty because it forms part of a country’s overall economic policy. The EU has no powers (competence) over direct taxation, only over indirect taxation – and then only if measures are approved unanimously at European level.54

In short, the financial and economic reconstruction of a country after a systemic bank collapse which then has to be financed by public taxes is an area that belongs to the competence of Member States. For this reason, it could be argued that the re-structuring and re-capitalisation of Icelandic banks after the crisis in 2008 fell outside the scope of EU/EEA law.

The conclusions for this section point in the same direction as in the previous case of State liability. From a legal point of view it would have been possible to put forward different arguments arriving at different conclusions. It is unclear whether the principle of non-discrimination by territory is equivalent to nationality, or whether this kind of prohibition applied in extreme circumstances due to the extreme gravity of a general financial crisis. The principle of non-discrimination could be trumped by other principles such as the lack of competence in EU law when a financial crisis and emergency circumstances jeopardise the economic sovereignty and financial stability of a country. Discrimination on grounds of territory could be justified in EU law only if the economic/financial future of a country was at stake. The truth is that this problem was a grey area not regulated by EU/EEA law at the time of the events.

IV. Other arguments of European law

1. Asymmetry of rights and obligations in European (financial) law unveiled by the lack of resolution of the Icesave dispute

The Icesave dispute is a good example of the deficiencies of the European internal market for financial services which were unveiled during the crisis. But, most seriously, it shows an asymmetry of rights and obligations in the EEA legal order that is highly questionable, both in the area of financial regulatory framework concerning consumer protection and concerning access to justice.

The rights of financial institutions to expand in the internal market have not been duly complemented by obligations on behalf of States and private economic operators. First of all, as stated above, while the Directive 94/19/EC stated that there must be a minimum guarantee for depositors throughout the EU and the EEA, there were no appropriate rules at European

52 Stefán Már Stefánsson, Articles published in the Icelandic newspaper Morgunbladid, supra note 25.

53 ECJ has declared that “... direct taxation falls within the competence of the Member States ...”; See ECJ, C-345/04, Contro Equestris [2007] ECR I-0142 at para. 19.

54 In the new Irish Declaration annexed to the Lisbon Treaty it is stated that the EU will have no new competences on taxation.
level for central supervision, or any instructions for the coordination at European level on emergency cross-border situations, no crisis management and certainly no system for requesting assistance or solidarity from other DGS schemes in the event of an extreme financial crisis. The case of a systemic bank failure in one EEA State exporting insolvency problems to other EEA States has never been foreseen in European law. As the Centre for European Reform puts it, "the crisis has exposed the weakness in the EU regulatory system and has reinforced the case for a serious reform of the institutions of global economic governance." These fundamental uncertainties on the most essential topic of European banking and financial law with regard to the consumers have been annotated by the doctrine and acknowledged by the EU institutions. They are precisely the reason why the European Commission has been revising the legal framework during 2009 and 2010.

European rules on the financial supervision and regulation of DGS proved inadequate in the light of the events of 2008/2009. Financial supervision rules were not suitable for covering the risks to consumers deriving from the broad expansion of banking firms within the EU/EEA. The EU regulators, and by extension the national regulators, did not correctly cater for the needs of the internal market. Banking activities crossed frontiers and established branches in other guest countries under the "home passport" rule while regulatory and financial supervision followed the rule of the home country and naturally remained fragmented. Supervision in guest states receiving branches from other home EEA States for reasons of financial stability proved to be ineffective. There was no role assigned in cross-border cases to the different European central banks or to the European Central Bank, nor any explicit rules for guarantees of last resort. For instance, there never seemed to be any reason to provide rules covering the cases of small countries outside the euro area when banking activities expanded to other EU/EEA countries for a value of ten times their GPD, as had happened in Iceland.

Furthermore, from a legal perspective, there is also an imbalance in Iceland’s rights and obligations in the diplomatic approach to this dispute. As these have been tackled so far on a bilateral basis at political level, the main problem still pending is the lack of access to justice for a State in a dispute that lives at the intersection of the EU Treaty and the EEA Agreement. In cross-border disputes between the EU and EEA countries, there is no direct competence for the ECJ or the EFTA Court if States do not come to agreement on direct actions. This has meant in practice that Iceland has been deprived of its right to effective judicial remedy in European law.

Whatever the reason or the economic or political arguments, this lacuna in the EEA Agreement, together with the legal uncertainties of EU banking and financial law, has been extremely prejudicial for Iceland. In EU law, any country could have started an infringement case questioning a certain interpretation of Directive 94/19/EC. Iceland, on the other hand, was pressed to accept the principles of State liability and nationalisation of private debt of banking entities abroad without being entitled in the subsequent clause agreements to any proper judicial and independent review of its legal arguments. Icelandic citizens do not have direct access to justice to the ECJ either. The agreements signed with the UK and the Netherlands forced Iceland to waive its rights to judicial review as well as its sovereign immunity for all its public assets.

Since the core of the dispute is located in EU/EEA law, we should be consistent and maintain a balance of rights and obligations under European law:
- either we decide that EU/EEA law does not relate to the hard core of this dispute and therefore both State liability and discrimination claims were trumped by emergency reasons of extreme gravity, touching the economic independence of a country, falling outside the EU/EEA Treaties.
- or we decide that EU/EEA law relates to the hard core of this dispute and gives States and individuals a proper system of judicial remedies and an opportunity to defend a case before a European court.

Any diplomatic strategy based on bilateral negotiations which imposes a certain interpretation of EU law to Iceland without providing a proper redress mechanism by an independent judge and a fair trial

55 Centre for European Reform, "Beyond banking: What the financial crisis means for the EU" (ECPS, Policy brief 2008); document available on the Internet at <www.cer.org.uk> (last accessed on 21 July 2011).

56 Different documents were produced by or under the supervision of the European Commission on the necessary reform of the Directive 94/19/EC where the liability of the State for the sufficient provision of funds under the DGS home country national scheme was never stated. All documents from the European Commission available on the Internet at <http://ec.europa.eu/internal_market/bank/guarantee/index_en.htm> (last accessed on 21 July 2011).
appears to be a somewhat strange conclusion in the field of European law integration. The nationalisation of private debt created by the collapse of the banking system endangering the economic future of a small nation, without the possibility for this nation to expose its legal arguments before a court of justice, does not appear legitimate when seen in the light of the European Treaties, the EU Charter of Fundamental Rights and the European Convention of Human Rights (ECHR). However, it is irrelevant to assign blame for the methodology, but the EU Treaties do impose on the EU institutions the duty to respect fundamental rights, the rule of law and to promote the European integration. And the ECHR also imposes obligations on European countries to respect fundamental citizens rights. In view of all the arguments given above, it seems reasonable to conclude this section with the following suggestion. While – for political and economical reasons – a diplomatic approach can be continued, and it is possible to sign an agreement and reimburse the UK and the Netherlands for the minimum guarantee given to depositors and therefore comply in principle with the claims under EU/EEA law, it can never be recommended nor accepted from a legal point of view that Iceland should renounce its right to take the issue of the immunity/liability of the Icelandic State and the use of the terrorist legislation by the UK against Iceland to either the ECJ or the EFTA Court. Unfortunately, the three countries must agree in order for any of these courts to take this matter up, which does not seem to be the case for the time being. The only possibility left was for the ESA to initiate an infringement proceeding against Iceland or that a resident in Iceland should introduce a national case before a domestic judge requesting an advisory opinion from the EFTA Court; but this is very difficult in Icelandic procedural law due to strict requirements for individuals to acquire proper legal standing to be able to take direct action and sue.

2. General principles of EU law – Balancing the doctrine of effectiveness of European law, fundamental rights and international social justice

The dispute over Icesave deposits has been treated with a perspective focusing narrowly on the meaning of the normative provisions of the Directive 94/19/EC. It is a principle established by the jurisprudence of the ECJ that EC law must always be interpreted taking into account all general principles of the EU legal order; it places European law in context.57

If the dispute over Icesave is examined in a Europe-wide context, in the light of other political, historical, philosophical and economical factors, one may even advance other essential arguments that should be taken into account when evaluating the final justice and fairness of the solutions discussed. Many questions which arise from the Icesave dispute are very difficult to answer because they force us to choose between a legal positivist approach where a rule is interpreted in a vacuum without consideration for the final justice of the solution reached (formal justice) or, on the contrary, a legal realist approach based on the whole set of principles of the EU legal order, where law is interpreted with a European perspective and general principles of law while searching for fairness of results (substantive justice). And the main questions which remain pending are the need for a sovereign guarantee vs. other legal possibilities recognised by ordinary bankruptcy law, and the scope and limits of the doctrine of effectiveness of European law.

In the first place, why is a State guarantee needed? Why is it not possible for Iceland to approach this dispute through bankruptcy law? This question was unresolved in Icesave 2 as the UK and the Netherlands have refused to claim directly the assets of Landsbanki in the UK/The Netherlands in bankruptcy proceedings, as they prefer to request a sovereign guarantee from Iceland for all deposits in order to avoid uncertainty. Icesave 3 admitted this approach to a certain degree. A quote from Martin Wolf, Chief Economist Commentator, Financial Times:58

"Asking a people to transfer as much as 50 per cent of GDP, plus interest, via a sustained current account surplus is extraordinarily onerous. Against this, the UK government argues that it is offering a lengthy grace period and an interest rate that is close to the cost of funding for the UK Treasury."
It also argues that as much as 90 per cent of the repayment it seeks could come from liquidation of Landsbanki’s assets. J—
Yet the obvious answer to the latter point is this: if the assets of the bank are that valuable, why not write off the debt, in return for the claims on these assets?"

And secondly, should Iceland as an EFTA/EEA State or the other EU Member States comply with a goal of the Directive 94/19/EC with a sovereign guarantee if this is going to place the nation in a situation of great financial debt and economic stress? Which should prevail: the specific goal of the EU Directive or the Preamble and the fundamental values of the European Treaties? While the Directive 94/19/EC gives an individual right to depositors regarding the immediate availability of their savings, should this right prevail over fundamental European principles such as the rule of law, fundamental rights, solidarity and social justice — all values proclaimed by the EU?

European integration is about solidarity between European states and peoples. If European law is put into context, a declaration that the effectiveness of European law and the rights of depositors should prevail over the economic sustainability of a country is a task that only the ECJ or the EFTA Court could enact without risking political, legal and ethical questions. As Petersmann notes, together with a ‘conservative function’ of judges to uphold ‘legality’ by applying existing rules of law, judges are also able to review whether the particular circumstances of a dispute may require other kind of ‘equitable’ dispute settlements. This is the classical tension between law and justice, between the letter of a legal provision and the justice of the final result. And the result obviously depends on judicial interpretation. As Petersmann explains, judges should avoid the ‘mismatch of justice’ provoked by a narrow interpretation of legal provisions. “By ‘giving reasons’, courts of justice contribute to the clarification of ‘public reason’ and to its continuous adaptation to changing public conceptions of justice.”

Justice and law should work together but this is not automatic in all circumstances and in all cases. As Petersmann has summarised, ‘conceptions of international justice’ in transnational relations among individuals as well as among states tend to be even more controversial than inside countries.” In his view, we should aim for the establishment of a transnational rule of law based on the principles of justice and respect for freedom, equality, and fundamental human rights. In this system that he envisions, the role of the courts is essential to guarantee good cooperation between different constitutional actors and reciprocal respect for their respective jurisdictions and constitutional foundations.

As stated above, the Icesave dispute is taking place in a wider European context, in the light of other political, historical, philosophical and economical factors. The methodology which is currently used to solve this dispute raises fundamental questions about law and justice in the European legal order that cannot simply be set aside.

The present study does not overlook the fact that the Icelandic Administration and Government do share substantial responsibility for the present situation. The sustainability and the risk management of the Icelandic banks in cases of emergency situations should have been better assessed. However, the failure of the Icelandic legal order should be properly analysed and assessed, avoiding oversimplification. The potential liability of Iceland does not exclude other liabilities.

If we consider the uncertainties of the State liability doctrine in the Directive 94/19/EC, if we explore the national rescue measures of nationalisation adopted by other EU countries (specially Ireland), if we set aside a black-letter approach to the Icesave dispute and put it in the framework of the values that lie behind the whole process, dynamics and principles of the European integration it is then very difficult to assert that the Icesave agreements between Iceland, the UK and The Netherlands have so far resulted in a fair settlement for the Icelandic nation.

Why is this so? Because the terms of these Icesave agreements defy the essential principles of the European legal order. First, they were international (business) law contracts strongly biased in favour of the lenders, which reflected a fundamental mistrust of Iceland and its legislative, executive and judicial powers. Secondly, they did not allow Iceland to take this dispute before the ECJ under EU/EEA law, and deprived Iceland and Icelanders of access to justice. But, thirdly and most importantly, Iceland was obliged to

waive its sovereign immunity so that, in the event of non-compliance of the payments, the creditors could seize national assets such as schools, hospitals, public companies, etc. While Iceland agreed with the Icesave Act 1 for reimbursing the debt towards the UK and The Netherlands insurance funds which anticipated the guarantees to the depositors, the Icesave agreements jeopardised the country’s own economic future and recovery. That is the reason why the Icelandic Parliament approved Icesave 1 with certain reservations.

Essential questions of European law still remain unanswered. Citizens, lawyers and institutions still do not know whether the State of Iceland was negligent by comparison to other EU countries in the implementation of the Directive 94/19/EC during the financial collapse of its banking system.\(^{62}\) It is still unclear whether or not the alleged discrimination on the basis of territory is acceptable in the case of exceptional financial circumstances, or whether a sovereign guarantee from Iceland is absolutely needed to finance the payment of the debt. These uncertainties make the Icesave Agreements 1, 2 and 3 very difficult to accept for the Icelandic society.

V. Conclusions

From a European legal perspective the dispute and settlement of the Icesave dispute is highly complex. It presents difficult choices derived from diverse legal, economic and political factors.  

1. The State liability of Iceland resulting from the Deposit Guarantee Fund (Tryggingasjóður) not having sufficient funds to cover all depositors is very unclear under the Directive 94/19/EC. In spite of the legal opinions of the EU/EEA institutions, European law did not at the time provide a clear, definite and obvious answer. An oversimplification of liability has resulted in Iceland assuming all responsibility.

2. It is still unclear whether the principle of non-discrimination of European law is also applicable on grounds of territory or whether depositors abroad were in a situation comparable with domestic depositors.

3. The EU has no competence regarding national measures designed to nationalise, bail out or restructure domestic banks in emergency situations such as the recent financial crisis demanded. Does the reconstruction of the whole banking system of Iceland fall outside the scope of EU and, by extension, EEA law? If neither the EU nor the EEA has any competence in the issue, the principle of discrimination does not come into play.

4. The Icesave dispute dramatically unveiled a grey area of European law in the field of financial services and is the paradigm of the current financial reform. EU/EEA law did not provide at the time a legal framework to manage or stop or help during the Icelandic crisis.

5. Under all circumstances, analysis of the legal dispute and the interpretation of European law should not be limited to discussion of the normative provisions of Directive 94/19/EC in isolation, as there is a political, economical, sociological and even ethical context to European law.

6. In order to come out of the current impasse, suggestions for progress in the resolution of this dispute could be based on a pragmatic approach towards law and diplomacy. Iceland could accept a diplomatic agreement pending the discussion of all legal issues before the competent European court.

7. In spite of declarations of the EU and Icelandic governments to the contrary, Icesave is one of the main reasons why Icelandic citizens have lost faith in European integration and are now sceptical about accession. At the same time, secret documents not yet released to the general public request that Iceland honour its Icesave obligations to allow it to join the EU. A perverse dynamic is taking place where all actors of the Iceland-Europe drama seem to be trapped in an impossible situation.

8. Postscriptum: The situation in August 2011 is the following. On June 10, 2011, the EFTA Surveillance Authority ruled that Iceland is obliged to ensure payment of the minimum compensation to Icesave depositors in the UK and the Netherlands, according to the Deposit Guarantee Directive 94/19/EC within 3 months. The Authority does not accept the arguments of the Icelandic government, sent in a letter of 2 May 2011. Iceland’s position is that the obligation concerning the deposits does not involve a State guarantee. While there is nothing in ESA’s reasoned opinion to alter this position, Iceland has nevertheless until 10 September 2011 to pay 670 billion ISK. The assets of

\(^{62}\) Letter from Commissioner Michel Barnier, supra note 7.
Landsbankinn are supposed to cover most of the debt but, in fact, no payments can be made before the Icelandic Supreme Court has ruled on legality of the 2008 Emergency Law. Should Iceland not comply, the EFTA Surveillance Authority will consider taking the case to the EFTA court. Iceland's chances in EFTA court are difficult to assess. A victory might prove though a mixed blessing: setting a new precedent in international/European banking but scaring investors away from Iceland.
SYMPOSIUM ON THE FINANCIAL CRISIS IN THE EU
(PART 1)
Transparency Regulation in Financial Markets – Moving into the Surveillance Age?
Iris H-Y Chin
A Crisis of Governance? From Lamfalussy to de Larosière
Despina Chatzimanolis
Origination and Distribution of Debt: Risks and Regulatory Solutions
Anselm Lenhard
The Icesave Dispute in the aftermath of the Icelandic Financial Crisis
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ARTICLES
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Michael Faure and Louis Visser
China’s Milk Scandals and Its Food Risk Assessment
Institutional Framework
Piqian Li, Xiao

REPORTS
Towards A Unitary Patent Protection System
Enrico Bonadio
“One to rule them All”? – The Standardisation of Nanotechnologies
François Thureau
Cognitive Neuroscience, Decision Making and the Law
Balfour Botulica
US–Poultry from China – Just Another SPS Case?
Lukasz Gruszczynski
Contents

Editorial
Alberto Alemanno 301

SYMPOSIUM ON THE FINANCIAL CRISIS IN THE EU
(PART 1)
Editorial
Giorgio Tosetti Dardanelli 303
Transparency Regulation in Financial Markets – Moving into the Surveillance Age?
Iris H-Y Chiu 305
A Crisis of Governance? From Lamfalussy to de Larosière or Bridging the Gap
Between Law and New Governance in the EU Financial Services Sector
Despina Chatzinikoli 322
Origination and Distribution of Debt: Risks and Regulatory Solutions
Anselm Lenhardt 340
The Icesave Dispute in the Aftermath of the Icelandic Financial Crisis:
Revisiting the Principles of State Liability, Prohibition of State Aid and Non-Discrimination
in European Law
Maria Evira Méndez-Pinedo 356

ARTICLES
Life and Nuclear Radiation: Chernobyl and Fukushima in Perspective
Wade Allison 373
The Role of Experts in Assessing Damages – A Law and Economics Account
Michaël Faure and Louis Visscher 376
China’s Milk Scandals and Its Food Risk Assessment Institutional Framework
Pinghui Xiao 397

REPORTS
Biotechnology
The Transition to a New EU Plant Protection Regime – Legal Problems in the
Regulatory Field
Gérardine Garçon 407

Food
Failure of Conciliation Talks on the Use of Animal Cloning for Food:
“The Consumer’s Right to Make Informed Food Choices”
Marie Frient-Perrot and Lise Rihouey 414

Intellectual Property
The EU Embraces Enhanced Cooperation in Patent Matters:
Towards A Unitary Patent Protection System
Enrico Bonadio 416

Nanotechnology
“One to Rule them All*? – The Standardisation of Nanotechnologies
François Thoreau 421

Risk Communication
Cognitive Neuroscience, Decision Making and the Law
Barbara Bottalico 427