



Bail-In

An Icelandic perspective

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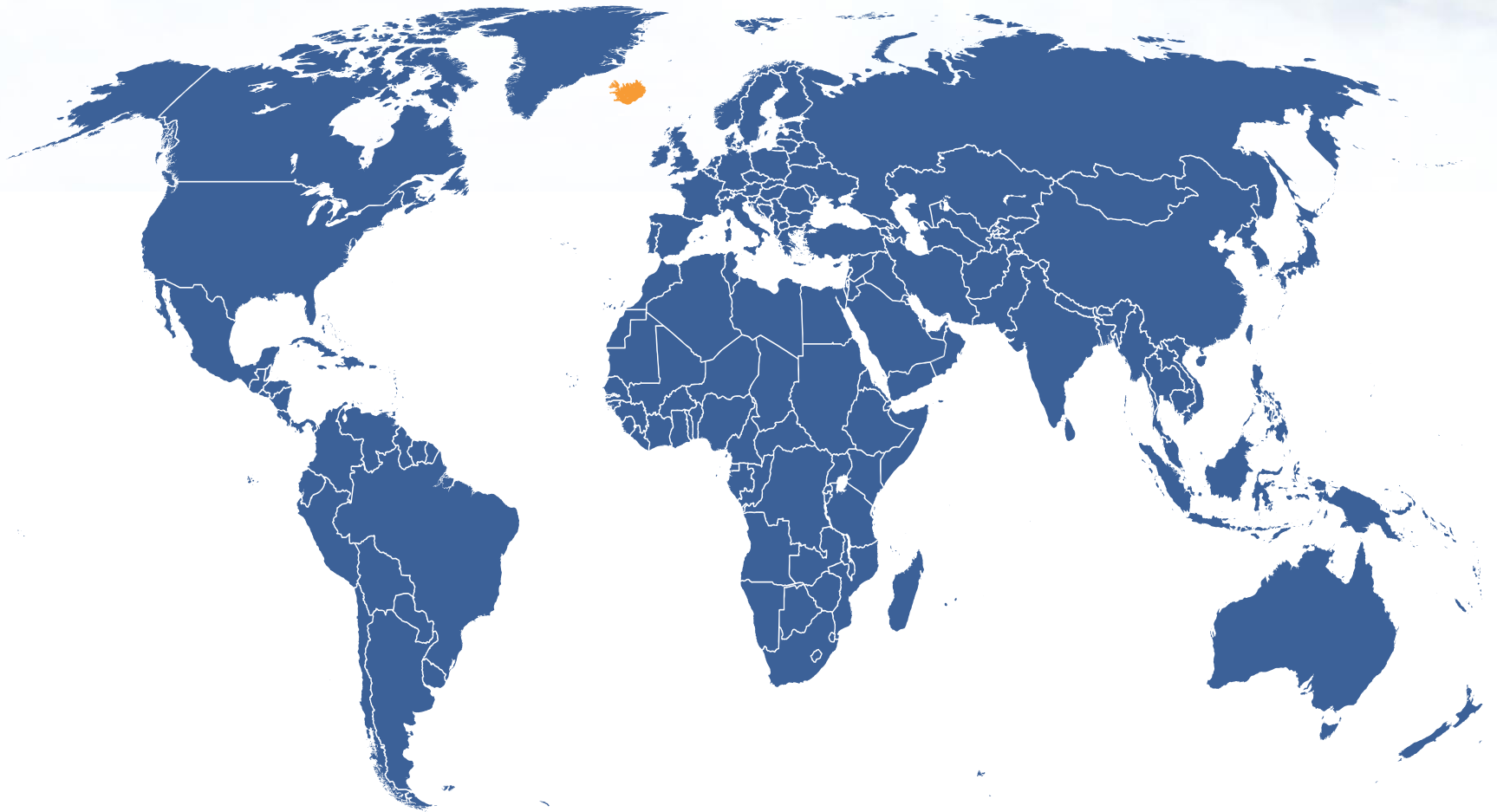
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ICELAND

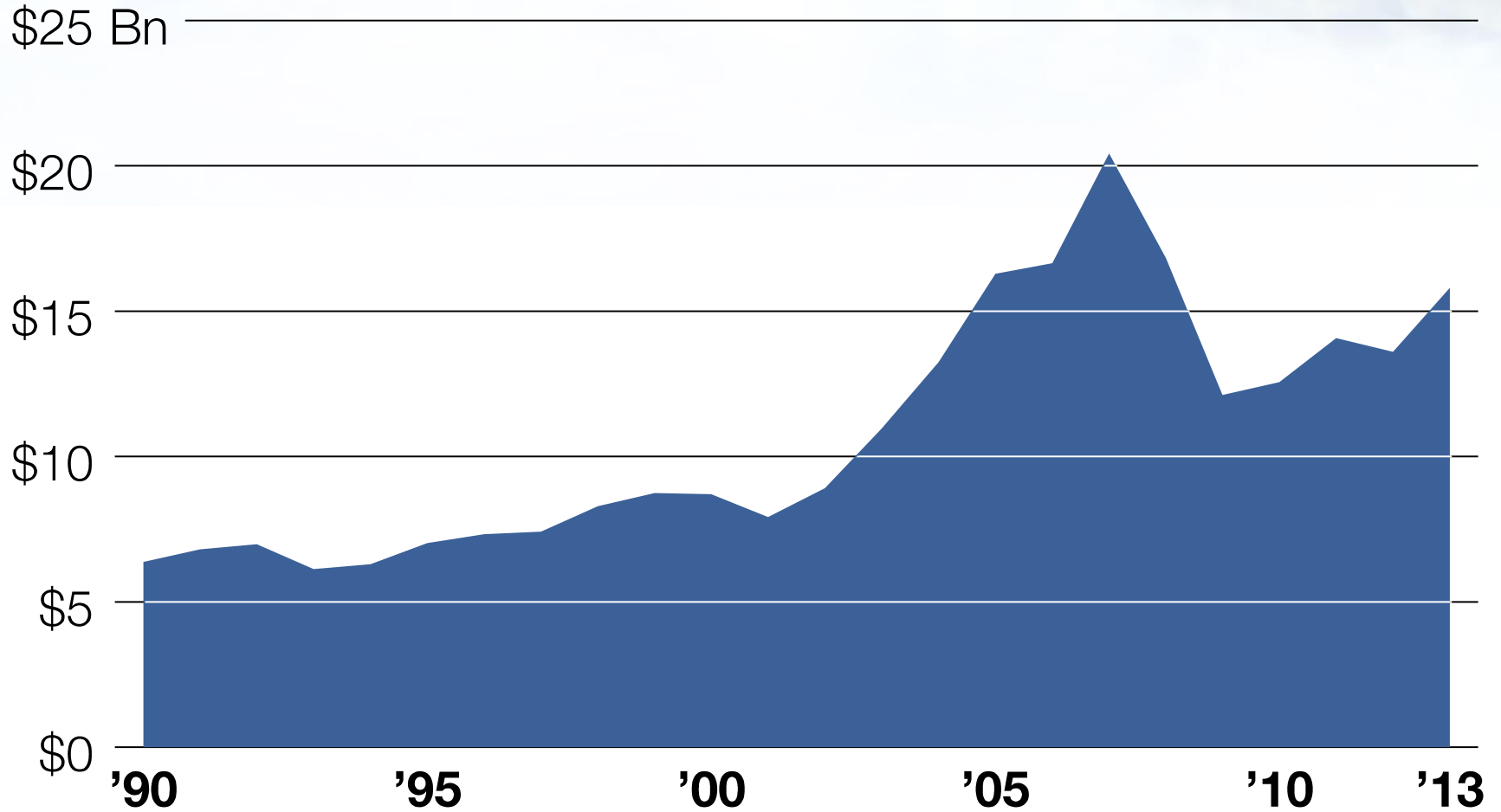




Population

320,000

Historical GDP



International Status

- **European Economic Area — Single Market**
(EU plus Iceland, Liechtenstein and Norway)
- **Iceland adopts most EU legislation concerning the four freedoms, including all legislation on financial services**
- **International cooperation**
 - United Nations
 - Human Rights Convention
 - EFTA
 - OECD
 - NATO

Regulatory Background

- Icelandic Depositors' & Investors' Guarantee Fund (DIGF) founded in 1999 as required by EU directives.
- Supervised by the Icelandic Financial Supervisory Authority.

Icelandic Banking Bubble

- Liberalisation
- Privatisation
- International Credit Bubble
- Foreign Expansion





CRASH

2008

CRASH

2008

- Access to international liquidity evaporated
- Banks' liabilities 10 times annual GDP
- CBI unable to provide liquidity

CRASH 2008

- All big three Icelandic banks failed
- In the end, 99% of financial institutions in Iceland either failed or were restructured

COMPLETE SYSTEMIC CRISIS

Devils & Deep Blue Sea

- Domestic monetary system in grave danger
- External assistance unreliable
- Liabilities too large for the state to absorb
- Bailout credibility negligible
- Taxpayers unwilling to foot the bill
- Social cohesion risks visible

Icelandic response

- Emergency Act of Parliament
 - Intervention powers of FSA
 - Deposit preference
 - Bail-In of sorts
- Political guarantee of all deposits
- Capital Controls
- IMF programme

Only a Bail-In of sorts...

- Legislation not negotiation
- Many creditors immediately dumped claims
- Not all creditors were equal
- Limited patience of “Vulture Funds”
- Capital controls locked in \$8 Bn of debt

The Icelandic Bail-In

- Failing banks placed in Resolution Regimes
 - Old banks held on to foreign assets
 - Deposits given priority status
- New domestic banks carved out
 - domestic loan book of the old banks (1.7xGDP)
 - Domestic deposits
 - Compensation to old banks for difference

Moral Hazards of the Icelandic Bail-In



- Measures taking immediate effect (some would say retroactive)
- Division of assets and liabilities raised questions
- Danger of future assumptions

Practical lessons learnt

- Bail-Ins are preferable to Bailouts
- Have clear legal framework in place
- Define regulatory powers precisely
- Insure judicial oversight
- Avoid differential treatment of creditor classes

Thin fine line of the Law

- Legislation should not be too specific
 - Every eventuality cannot be anticipated
 - The law must not be too rigid and formalistic



- Legislation must not be too vague either
 - Most important that the objective of the act and basic principles are as clear as possible

Practical lessons learnt

- Put timeframes in place and enforce them
- Banks accumulating assets through enforcement of lien
- Managing conflicts:
 - Time constraints
 - Competition
 - Independence
 - Open sales process
- Dedicate resources to details and seek International consultation
- Emphasize clear and candid communication with stakeholders as well as with the public and press.



**No pain,
no gain.**

Thank you