Inside story: Iceland

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In the autumn of 2008 the Icelandic financial system faced severe difficulties. The failure of the country's three largest banks, Kaupthing Bank ("Kaupthing"), Glitnir Bank ("Glitnir") and Landsbanki ("LBI"), led to them being taken over by the Icelandic Financial Supervisory Authority under new powers granted by Act No 125/2008 on the Authority for Treasury Disbursements due to Unusual Financial Market Circumstances. The legal framework for dealing with the insolvency of banks and other financial institutions in Iceland is set out in Act No 161/2002 on Financial Undertakings (the "Financial Undertakings Act"), and Act No 21/1991 on Bankruptcy etc. (the "Bankruptcy Act").

Icelandic law was in many ways inadequate to deal with bankruptcies on such a scale. Consequently, the legislature needed to act to address a number of issues. The Financial Undertakings Act has been amended several times since October 2008, including to implement Directive 2001/24/EC, on the reorganisation and winding-up of credit institutions ("the Directive"), in accordance with Iceland's treaty obligations.

The Icelandic Banks' winding-up proceedings have raised a number of important issues in relation to cross border insolvencies and the recognition of winding-up measures in relation to financial institutions between Member States of the European Economic Area ("EEA"). One such issue led to the judgment of the European Court of Justice in LBI hf. v. Kepler Capital Markets SA, Frédéric Giraux, (Case no. C-85/12). This case concerned the recognition in other Member States of the EEA of the substantive winding-up proceedings in relation to LBI which, as a matter of Icelandic law, had commenced on 22 April 2009, without any judicial or administrative action.
LBI had been granted a moratorium by the Reykjavík District Court, on 5 December 2008. On 22 April 2009, Act No. 44/2009 came into force, amending Chapter XII of the Financial Undertakings Act, introducing (in point II) transitional provisions which applied the effects of certain substantive rules on winding-up proceedings to financial undertakings which were already subject to a moratorium.
The case considered the effect under the Directive of this decision of the Icelandic legislature to have the rules on winding-up proceedings apply during the moratorium period and, in so doing, to provide for the de facto commencement of winding-up proceedings, without this being based on a ruling by a court or other competent judicial authority.

1) Background of the case

a) Kepler Capital Markets SA ("Kepler") was a wholly owned subsidiary of LBI.

b) On 10 November 2008, Giraux, a French resident, had two attachment orders (í: kyrrsetning) served on Kepler, in order to guarantee payment of his claim against LBI.

c) On 5 December 2008, the Reykjavík District Court granted LBI a moratorium, in accordance with Law No 161/2002 on financial institutions.

d) LBI sought to have the attachment orders lifted, on the basis that under Article 138 of the Bankruptcy Act, enforcement action taken after 15 May 2008 (being the date six months prior to 15 November 2008, which was the reference date for LBI's moratorium) was null and void. Accordingly, under Icelandic law, the attachment orders had no effect.

e) Both the Regional Court of Paris and the Court of Appeal in Paris dismissed LBI's application. LBI appealed the decision to the Cour de cassation, which referred two questions to the ECJ:

2) First question: Was the winding-up of LBI which was commenced by the enactment of Act 44/2009 a measure adopted by "an administrative or judicial authority"?

i) The first question to be considered by the ECJ was whether the winding-up procedures which, pursuant to Act 44/2009, applied to financial institutions in Iceland which were the subject of an existing moratorium, constituted "measures adopted by an administrative or judicial authority" within the meaning of Articles 3 and 9 of the Directive.

ii) In answering that question, the Court looked at the aim of the Directive, namely to establish mutual recognition by Member States of the measures taken by a Home Member State to restore to viability credit institutions authorized in that Home Member State (recital 6) and equal treatment of creditors (recital 16).

iii) The Court noted that LBI's moratorium enabled the company to reorganize its financial situation, given its financial difficulties, and would therefore constitute a "reorganization measure" under the Directive. The question was however whether point II of the transitional provisions of Act No 44/2009, which amended the legal effects of that moratorium, by making financial institutions under moratorium subject to a specific winding-up scheme, would be regarded as such a measure.

iv) In answering that question, the court took account of the fact that the transitional provisions in point II of Act No 44/2009, which put LBI, Kaupthing and Glitnir into a winding-up procedure, only applied to financial institutions that had previously been granted a moratorium by a judicial decision.

v) The court also noted that the transitional provisions in point II of Act 44/2009 comprised a change to the substantive rules of the moratorium, which had come into effect pursuant to a judicial ruling. The Act did not order the winding up of the financial institution as such; it merely amended the legal effect of the existing judicial decision which granted the moratorium.

vi) The Court further noted that the District Court of Reykjavik had made a ruling on 22 November 2010 confirming the winding-up proceedings in relation to LBI, so the winding-up of LBI was not based solely on the transitional provisions in point II of Act 44/2009.

vii) In light of the above, the Court concluded that LBI's winding-up proceedings under Act 44/2009 had been adopted by "administrative or judicial authority" for the purposes of articles 3 and 9 of the Directive.

3) Second question: Does Moratorium prevent measures being adopted against a company in another Member State?

i) Does Article 32 of the Directive preclude the moratorium (which prohibits or suspends legal action against a financial establishment) from having effect to prevent interim protective measures being taken in another Member State? What about measures taken before the declaration of the moratorium?

ii) The Court noted that the lex concursus of the Home Member State (Iceland) would govern the reorganisation measures and the winding-up procedures and the effects of those measures would be established according to the laws of that Home Member State.

iii) The Court noted that with regard to winding-up proceedings, Article 10(2)(e) of the Directive states that "proceedings brought by individual creditors" are subject to the law of the Home Member State, with the exception of, effects on "lawsuits pending". The court found that this latter exception to the general rule must be interpreted strictly

iv) In determining the interpretation of Article 32, the Court look at recital 30 in the preamble to the Directive, which makes a distinction between a "lawsuit pending" and an "individual enforcement action", since a "lawsuit" pending would be governed by the law of the Member State in which the lawsuit is pending, but the "individual enforcement action" would be governed by the law of the Home Member State.

v) The Court concluded that protective measures, such as the attachment orders sought by Mr. Kepler, constituted individual enforcement actions. By prohibiting or suspending those actions, the moratorium did not therefore fall foul of Article 32 of the Directive as those actions were governed by Icelandic law as the lex concursus.

vi) The Court also concluded that the fact that Mr. Kepler's measures were adopted before LBI's moratorium came into effect would not alter this conclusion, since the lex concursus would also govern the temporal effect of the reorganization measure and of insolvency proceedings.

4) Conclusion

The ECJ preliminary ruling therefore concluded that

i) The Bank's moratorium is a reorganisation measure according to the Directive,

ii) the bank's winding-up procedure is with a reorganisation or winding up measure within the meaning of articles 3 and 9 of the Directive, both before and after the court ruling of the bank's winding-up in November 2010,

iii) that court cases that had started before the bank's moratorium, and which were not individual enforcement actions (such as attachments orders) would be governed by the law of the Member state where those actions had been brought, and

iv) Individual enforcement actions (such as Mr. Kepler's attachment orders) would be governed by Icelandic law and therefore automatically annulled in accordance with Article 138 of Law on Bankruptcy No 21/1991.