

GFSC clarifies misconceptions over Landsbanki Gsy collapse

MISCONCEPTIONS about the collapse of Landsbanki Guernsey need to be laid to rest, according to the Guernsey Financial Services Commission.

Speaking exclusively to the Guernsey Press ahead of the expected publication in early December of Promontory Financial Group (UK) Ltd's inquiry into how the regulator handled the banking crisis, GFSC chairman Peter Harwood, pictured on the right, and director-general Peter Neville, pictured left, have spoken out.

Mr Neville said many misconceptions about the Landsbanki situation had developed wildly ever since the bank was placed into administration on 7 October and they were simply not true.

The main thrust of them could be broken down into the following three categories:

- The GFSC did not do enough to stop the Landsbanki situation,
- The GFSC has not done enough since Landsbanki collapsed, and
- The GFSC had information that should have been communicated to depositors

However, Mr Harwood said speaking out now was in no way an attempt to cut across or pre-empt any of the conclusions to be made by the independent review team, which is headed by former Bank of England executive director Michael Foot.

'We are concerned at the number of misconceptions that have come out through letters we have seen,' said Mr Harwood.

'If we didn't address them, then they almost become written in stone.'

Two of the potentially most damaging and wide-of-the-mark rumours that began to spread in the days and weeks after 7 October were that Landsbanki Guernsey had transferred £36m. to its sister bank Heritable Bank in the UK the day before it was placed into administration, and that the GFSC had warned States departments to remove funds from Landsbanki before administration happened. Mr Neville said both were completely incorrect.

'It's simply not true to say we told States departments to take their money out of Landsbanki or Iceland.'

'No warnings were given to any States department or any third party.'

He said the GFSC only became aware that Landsbanki Guernsey could not survive during a meeting with its directors on the evening of 6 October, after which it was placed into administration by the Royal Court in the early hours of 7 October.

Mr Neville said the GFSC had done everything in its powers to stop Landsbanki Guernsey customers from suffering losses, but the extent, severity and suddenness of the global financial crisis were completely unpredictable.

This was coupled with the fact that the island had yet to establish a depositor compensation scheme despite the fact that the GFSC had been arguing in favour of one for a number of years.

He said looking back on the steps taken by the GFSC in the build-up to the Landsbanki collapse, it was difficult to see any other decision it could have



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taken along the way which would have averted the crisis.

The trouble with being a regulator, he said, was that when everything was going right they were said to be doing too much, but when things went wrong, they were accused of not doing enough.

'Regulators cannot be expected to be better at forecasting than other experts and step in to close down all risks without good reason.'

Had the regulator forced Landsbanki Guernsey to place all its assets in risk-free assets, for example, Mr Neville said the GFSC would have been criticised for being uncommercial and overbearing.

'We acted very quickly and firmly as soon as there was any threat on the basis of what was known at the time and what was reasonably foreseeable.'

'We have to take into account that if we act in the wrong way, for example by forcing a bank to do something that causes the public or other banks to lose confidence in the bank, we could cause the harm we are trying to avoid.'

By way of illustration, he said that the GFSC insisting the bank's balance sheet was restructured was not a popular decision with directors, because until that point in May 2008, 100% of funds were upstreamed from Guernsey.

'In early 2008, the worsening economic situation in Iceland did concern us and we asked Landsbanki Guernsey to restructure its balance sheet. At that time they were not happy because they said the action we were taking was much stronger than any other regulator.'

At that stage, Mr Neville said the GFSC thought the property loans in Landsbanki Guernsey and Heritable would have been enough to repay deposi-



tors. And it was following this restructuring of the balance sheet in May that the outlook for the group improved.

Between May and September, it was posting good half-year results and had a stable rating, but then the crisis hit with unprecedented haste at the end of September, which made it almost impossible for the GFSC to do anything that could then have stopped what eventually did happen.

'Our ability to act was constrained by the fact that, once the depth of the crisis became apparent on 29 September when the Iceland Government took over 75% of Glitnir, if we had taken such action it could well have caused the harm we were trying to avoid.'

Mr Neville said Landsbanki Guernsey had substantial liquid resources and it was believed that if it had to cut loose from its parent, Landsbanki Islands hf, it along with Heritable could stand alone.

'As substantial suppliers of retail liquidity, these two banks represented valuable assets that could be sold.'

And the takeover of Glitnir had falsely given the GFSC confidence that the Icelandic authorities would take appropriate action and rescue Lihf, Landsbanki Guernsey and Heritable if necessary.

'In the week before the collapse, the signals on Iceland were positive. It was only as late as 6 October, as far as we could establish, that acute liquidity issues emerged.'

Since then, Landsbanki Guernsey depositors have received 30p in every pound deposited with the bank, but are still waiting for news on the rest.

Mr Neville said he was committed to getting the best result possible.

'I would like to take enough action to get all the money back but I do believe we have taken the right action and as much action as we could as this thing developed,' he said.

Landsbanki Gsy figures at time of its collapse

Assets		Liabilities	
Liquid interbank placements	£41,266,000	Client liabilities	£117,330,000
Group placements:		Accrued interest	£3,321,000
Heritable Bank	£36,344,000	Estimated unsecured and preferred creditors	£530,000
Landsbanki Islands hf	£12,753,000		
Loan assets supported by UK property security	£52,449,000	Total liabilities	£121,181,000
Other assets	£549,000	Net assets	£22,180,000
Total assets	£143,361,000		

We have questions of our own, says GFSC head

THE GFSC also wants some answers of its own in relation to the run-up to Heritable's collapse on 7 October.

Peter Neville, GFSC director general, said the collapse of Landsbanki Guernsey's sister bank was just one of a number of issues the regulator was in discussions with the UK authorities about.

'There are questions to be answered about the run-up to Heritable being placed into administration the day after we placed Landsbanki Guernsey into administration.'

He said these would relate

to the freezing of assets and the transfer of retail depositors out of Heritable.

'They all went to ING Direct. This was done by the government and that raises the question of the treatment of the Guernsey depositors to the UK depositors.'

But Mr Neville said there was nothing wrong with Landsbanki Guernsey placing £37m. with Heritable, as it was a separate UK bank, with its own capital and balance sheet, supervised by the Financial Services Authority.

There was also nothing wrong with allowing the bank

to place £54m. in UK property loans because there were not enough lending opportunities in Guernsey to allow a loan book to be established.

He said the GFSC relied on the FSA's regulation and supervision.

'The GFSC was in very close contact with the FSA throughout the whole period leading up to the placing of funds with Heritable and subsequently, including at the time Landsbanki Guernsey was placed into administration.'

It is essential that regulators can depend on each other

in cross-border situations for information on current and potential problems and for co-operation in resolving problems.

'We have a memorandum of understanding with the FSA.'

'The Basel standards on bank regulation also require regulators to cooperate.'

However, Mr Neville said this did not mean there was still not a number of questions that needed to be answered in relation to Heritable's collapse, although he added at this time it would be inappropriate to comment any further on them.

Other misconceptions the GFSC wants to rectify...

1 Depositors were not aware of the takeover of Cheshire Building Society's Guernsey subsidiary in 2006 – **incorrect**. They were all written to individually in the summer of that year and a notice was placed in La Gazette Officielle.

2 The GFSC was wrong in permitting Lihf to take over Cheshire Guernsey – **incorrect**. Lihf was a top 500 bank – ranked 397 in the world at the time of permission being given to the takeover. By July 2008 it had moved up to 177. It met all the standards required and the acquisition also gave the Guernsey bank a future, which was otherwise in doubt. There was also a very strong letter of comfort from the parent company and there had been some very strong stress testing done at the time. It was also the strongest of all the Icelandic banks at the time.

3 The GFSC should have prohibited all upstreaming after the Northern Rock Guernsey incident – **incorrect**. Guernsey's banking model is partly founded on the basis of upstreaming. There would also have needed to be a clear threat to depositors to stop it and, if the GFSC had taken such an action, it believes it might have caused a crisis and been accused of being uncommercial, overbearing and heavy handed.

4 The GFSC has not been taking enough action since Landsbanki's collapse in getting depositors' money back – **incorrect**.

On 13 October the GFSC wrote to the Icelandic regulator calling on Lihf to honour the commitment given in its public undertaking to make any payments Landsbanki Guernsey could not make. This covers both the £12.75m. owed by Lihf and the £36.3m. owed by Heritable.

This letter has been followed up on several occasions demanding a reply.

In addition, joint administrators Rick Garrard and Lee Manning have continued to take the appropriate steps and Chief Minister Lyndon Trott has also written to the minister of finance in Iceland calling on the Icelandic Government to make sure Lihf honours its obligations.

All these calls to honour the obligations are now with the Resolution Committee set up in Iceland to resolve the banking crisis. The UK Government is also representing Guernsey's interests and those of the Landsbanki Guernsey depositors in negotiations it holds with the Icelandic Government.

5 The GFSC did not protect depositors because it confused its regulatory role with a promotional one – **incorrect**.

The GFSC does not have a promotional role at all. GuernseyFinance has promotional responsibilities for the island.

Key dates...

1997 Licensing of Cheshire Guernsey.

2006 September Acquisition of Cheshire Guernsey by Lihf to become Landsbanki Guernsey.

2008 May Landsbanki Guernsey diversified its balance sheet.

Late September/early October Following the Lehman Brothers collapse on Monday 15 September, interbank markets ground to a standstill and bank liquidity dried up.

29 September 75% of Glitnir taken over by Icelandic Government.

30 September Moody's places Landsbanki on review for possible downgrade.

1 October Landsbanki sold the majority of its overseas corporate finance and brokerage business to raise funds. The sale was cancelled on 10 October following the UK authorities' freezing of Landsbanki's UK assets.

6 October Icelandic Government passed an emergency law allowing the Icelandic regulator to take over banks.

6 October Directors of Landsbanki Guernsey decided to place the bank into administration.

7 October Heritable placed into administration and Landsbanki taken over by Icelandic regulator.

16 October It is announced Landsbanki Guernsey depositors will receive 30p in every pound deposited with the bank.