

Iceland: Lessons to be Learned from The Economic Meltdown

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In the wake of the failure of the Icelandic banks Messrs Brown, Barroso and Strauss-Kahn prove that they have understood nothing

From G8 to G20, many heads of state and government seem to delight in repeating that nothing will ever be the same again. The world is changing, to the point of being turned on its head by the crisis; the way we think and act in terms of financial regulation, international relations and development aid must therefore, according to them, change too. However, numerous examples contradict all this big talk. The situation in which Iceland now finds itself following the implosion of its banking system and the emergency nationalisation of its three main banks (Kaupthing, Landsbanki and Glitnir) is undoubtedly one of the most significant of these examples. This small country of 320,000 inhabitants is now reeling under the weight of billions of Euros of debt, which has absolutely nothing to do with the vast majority of its population and which Iceland cannot afford to pay.

I became interested in Iceland through my role as an adviser to the criminal investigation into the causes of the failure of its banks, which is at the root of its difficulties. However, I am not going to talk about that investigation, but something that goes far beyond it. In any case, I am by no means a spokesperson for the Icelandic authorities, whose responsibility in all this is clearly not insignificant. The previous government had even been dissolved due to public dissent over cronyism and the clannish running of institutions, which were seen as the cause of all of its problems. Moved by the fate of Iceland's deserving and likeable people, and the complete absence of discussion in the European media about what the future holds for them, I simply want to draw the attention of public opinion to the issues at stake in this case - major challenges that are not confined to the shores of this island. The irresponsible attitude of certain countries, the EU and the IMF to the collapse of the Icelandic economy demonstrates their inability to learn from the dramatic undermining of the model that it embodied: one of excessive deregulation of markets, particularly financial markets, that the majority of those same key players contributed to shaping.

Let us look, first of all, at the demands of the UK and the Netherlands. These countries are concerned by the failure of the Icelandic banks because they had welcomed their subsidiaries and branches with open arms, even though their authorities had been at least partially alerted to the risks hanging over those banks. They are now demanding that Iceland pay them astronomical sums (more than €2.7 billion to the UK and over €1.3 billion to the Netherlands), plus interest at 5.5%. They consider that Iceland was responsible for guaranteeing the funds deposited with Icesave, the internet arm of Landsbanki that was offering unbeatable rates. The British and the Dutch decided to set that guarantee not at around €20,000 per deposit, as provided for in European and Icelandic legislation- which

would already have been impossible for the Icelandic government, who quickly announced after nationalising its banks that it could only guarantee deposits made in Iceland itself – but at €50,000 to €100,000 per deposit, or even higher. Moreover, the measures that they are taking to get their way are scandalous.

Indeed, at the very start of October, the UK began with a measure of extreme retaliation: freezing of the assets of not only Landsbanki but also Kaupthing Bank, which was totally unconnected to Icesave, using its anti-terrorism legislation. In doing so, the UK lumped the Icelandic people, their allies in NATO, together with the likes of organisations such as al-Qaeda... And since then, it seems to be using all of its influence to ensure that no international aid is really given to Iceland until its demands have been met. Indeed, Gordon Brown told his parliament that he is working “with the IMF” to establish how much it considered the UK was entitled to claim from Iceland. The IMF itself, meanwhile, not content with putting off making its loans available to Iceland, attached conditions to them that would seem outrageous, even in fiction.

One example of this is the objective of bringing Iceland’s public deficit down to zero by 2013, a target that is impossible to achieve but that will nevertheless lead to huge cuts in the most essential areas of spending such as education, public health, social security, etc. Finally, on the whole, the attitude of the EU and other European countries has hardly been more commendable. The European Commission has clearly sided with the UK, as its President announced in November that there would be no European aid until the Icesave case had been resolved. It is true that Mr Barroso – too busy with his own campaign and terrified of upsetting his main source of support, London – is, as is often the case, in over his head. **Even the Scandinavian countries, which heralded international solidarity, are conspicuous by their lack of reaction to the blackmailing of Iceland – which certainly puts the generosity of the loans they have promised into perspective.**

Mr Brown is wrong when he says that he and his government have no responsibility in the matter. Firstly, Mr Brown has a moral responsibility, having been one of the main proponents of this model which we can now see has gone up the spout. But he also has a responsibility in the sense that he cannot really hide behind the legal status of Icesave – which made it formally dependent on the Icelandic banking authorities – and say that the UK had neither the means nor the legitimacy to supervise its activities. Could anyone realistically think that a handful of people in Reykjavik could effectively control the activities of a bank in the heart of the City? Moreover, it should be noted that the European directives concerning financial conglomerates seem to suggest that EU member states that allow such establishments into their territories from third countries must ensure that they are subject to the same level of control by the authorities of the country of origin as that provided for by European legislation. So, was there perhaps a failure on the part of the British authorities on this point, which would not be particularly surprising considering the ‘performance’ of other English banks (which were in no way related to Iceland) during the financial crisis? If so, Mr Brown’s activism in relation to this small country might be motivated by a wish to appear powerful in the eyes of his electorate and taxpayers, whose own losses cannot be played down. Of course, the Icelandic institutions have a great deal of responsibility in this matter. But does that necessarily mean that the – also considerable – responsibility of the British authorities should be overlooked, dumping it all on the Icelandic people alone?

Iceland, whose only remaining source of income is its exports, will certainly not be able to pay off those debts. The Icesave agreement, that the Icelandic parliament is expected to

vote on soon, would burden Iceland with a debt equivalent to £700 billion for the UK or \$5.6 trillion for the US. Nor will Iceland be able to clear its deficit in less than five years, when national deficits are rising more quickly than ever, even for the great powers – with the UK and the US once again providing two very good examples. Unless a radical new approach is adopted, Europe and the IMF are about to perform a major feat: reducing a country whose HDI had, in just a few decades, reached the highest level in the world, to the rank of a poor country... The consequence of this is that the Icelandic people, the majority of whom are highly qualified and multilingual and have strong work relationships with the Nordic countries where they can assimilate easily, are already starting to emigrate. In the end, neither the IMF, nor England or the Netherlands will be able to be reimbursed. Just a few tens of thousands of retired fishermen will be left in Iceland, along with its natural resources and a key geostrategic position at the mercy of the highest bidder – **Russia, for example, might well find it attractive.**

Even so, there are alternative solutions. Indeed, the countries of the European Union could have devised a mechanism that would allow them to consider their own responsibilities in this situation, to improve the regulation of financial markets and even take on at least part of the debt – which European legislation in no way prohibits – for having failed in their banking supervision role.

They could have offered to help Iceland, which obviously has no experience in the matter, with the investigation that it is seeking to conduct to try to understand what really happened and to thoroughly analyse the causes of this disaster. They could even have taken the opportunity to start their own debate about a European public prosecution service in charge of matters concerning transnational crime, particularly financial crime, which, once again, European legislation in no way precludes. The IMF and its Managing Director could also have taken this opportunity to thoroughly review the nature of the conditions that they attach to their loans. They could have made them more realistic, more focused on the long term, and made it possible to incorporate at least some social considerations. That would have been a first step towards true reform of multilateral institutions of this type and international solidarity procedures – and for Mr Strauss-Kahn himself, a chance to finally make his mark at the head of the IMF.

Engaging in this debate would obviously require a lot of time and energy, and a great deal of vigilance, particularly in the European Parliament, where discussions should be organised over the coming months. However, the Swedish presidency of the EU does not seem to be in a hurry to improve regulation of the financial sectors, and the committees with an economic focus in the Parliament are, more than ever, dominated by liberals, particularly British liberals. Yet the tools and levers for real progress are there; a catastrophe like that in Iceland could finally raise a meaningful international response, instead of the irresponsible and cynical pressures that we can still see today.

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