

**PROCEEDINGS OF THE
SELECT COMMITTEE OF TYNWALD
ON KAUPTHING
SINGER & FRIEDLANDER
(ISLE OF MAN) LIMITED
AND THE DEPOSITORS'
COMPENSATION SCHEME**

EPTKSF151110

Douglas, Monday, 15th November 2010

Morning Session: 10.30 a.m. – 11.46 a.m.

*The Committee sat in public at 10.30 a.m.
in the Legislative Council Chamber,
Legislative Buildings, Douglas*

[MR WATTERSON in the Chair]

Procedural

The Chairman (Mr Watterson): Good morning, everybody. Welcome to this latest session of the Select Committee on Kaupthing Singer & Friedlander.

As many of you know, we were established on 16th July 2009 with the remit to look at the cause of the collapse of Kaupthing Singer & Friedlander (Isle of Man) Limited, the role of the Financial Supervision Commission in ensuring the proper management of KSF (Isle of Man) Limited to protect depositors' funds, the credibility of the Depositors' Compensation Scheme, and any other relevant matter, and to report back by the March 2010 sitting of Tynwald.

The first part of the Committee's work has already been reported on, and that report went to the July sitting of Tynwald. We are now turning our attention to the second part of the inquiry and the credibility of the Depositors' Compensation Scheme and any other relevant matter.

Part of the inquiry will focus on the action to try and save Kaupthing Singer & Friedlander. We are, therefore, this morning, taking oral evidence from the Hon. Allan Bell, MHK, Minister for the Treasury at the time, and the Chief Financial Officer, Mark Shimmin. Further evidence sessions will take place in November

with the Liquidator and representatives of depositors' groups.

15 For those of you who are unfamiliar, I will just go around the table and do the introductions. To my far right is Mr Roger Rawcliffe, adviser to the Committee, Mr Phil O'Shea, adviser to the Committee, Mr Alan Crowe, who has just joined the Committee to replace Eddie Lowey, who has since joined Treasury. I am Juan Watterson, the chairman and, to my left, Roger Phillips, the Clerk to the Committee, and, to my far left, John Houghton, MHK, a member of the Committee.

20 I have already reminded people to turn their telephones off .

Could I ask if, Minister, and Mr Shimmin, you would like to make an opening statement, or would you like to go straight on to questions?

25 **Mr Bell:** I think it would probably be wise if we just go straight on to questions, Mr Chairman.

The Chairman: Okay.

30 **Mr Bell:** To begin with, I just want to apologise this morning. I have been ill for the last few days and I am still pretty ill this morning, so I might have to refer some of the questions to the only one of us who can speak at the moment.

The Chairman: Sorry to hear that. Thanks very much for joining us, anyway.

35

EVIDENCE OF HON. A. BELL AND MR M. SHIMMIN

40 **Q1060. The Chairman:** Basically, looking to some structure this morning and a few main themes. Firstly, the efforts that were made to ensure that KSF remained a going concern, despite the turmoil of 8th October; the efforts to ensure a 100% recovery for the depositors. Then we would like explore in a bit more detail the Scheme of Arrangement and then look at the Depositors' Compensation Scheme. So that is our plan, if you will.

45 If I can open up, then, by asking: why did the Government get involved after 8th October? The Liquidator Provisional had been appointed, Kaupthing Singer and Friedlander was heading into liquidation, why did the Isle of Man Government get involved?

50 **Mr Bell:** I think there was obviously a great deal of concern about the impact of this collapse, politically as well as broader, and it was vitally important – because Government had the Depositors' Compensation Scheme at the time to consider – that we got involved at an early stage to see what could be done to rectify the situation.

55 **Q1061. The Chairman:** And after the collapse, and various authorities came to the fore – the Liquidator Provisional, the directors of the company and Government – who was in charge of managing the whole situation?

Mr Bell: Well, shortly afterwards, the Chief Minister set up a steering group, and he chaired the working group, which consisted of representatives from Treasury and our various advisers.

60 **Q1062. The Chairman:** So the key decisions were being made by the Chief Minister –

Mr Bell: By the Chief Minister and his working group during that period, yes.

65 **Q1063. The Chairman:** Okay, I am conscious of the fact that we are not going to get into names of potential bodies that came forward at that time to rescue the Bank, for reasons of commercial confidentiality, but what discussions were held immediately following the collapse to find a buyer? Where did that process start?

Mr Bell: There was a belief – and one we still hold, in fact – that the Bank itself was solvent at the time it went under. It was brought about by a set of circumstances off Island which ultimately led to its demise.

70 Therefore, there was a belief commercially that there were elements – if not the whole Bank, certainly
elements within the Bank – that could be salvaged... therefore discussions started, I think, or contacts were
made, at a very early stage to see whether there was an option to consider...

75 **Q1064. The Chairman:** And these were bodies on and off Island –

Mr Bell: Yes.

The Chairman: – who credibly could have taken the Bank on?

80 *Mr Bell:* On and off, yes.

Q1065. The Chairman: And how were they identified? Was there a bit of a Treasury trawl of picking up
the phone, or were people knocking on your door, just waiting to buy a piece of KSF?

85 *Mr Shimmin:* I think the latter is more accurate. It was a case of people who saw an opportunity to either
buy the Bank or look at the assets of parts of the Bank and approach Government with proposals.

Q1066. The Chairman: What were the major obstacles to that happening in a timely manner?

90 *Mr Bell:* I think one of the major problems we had, for all that early period, was the lack of clear
information as to what the full value of the assets were, the situation of the assets held in the UK and the
length of time it was taking to identify what the potential outcome of those might be.

95 **Q1067. The Chairman:** It Government felt that this was a solvent bank that was just having a few
difficulties because of its relationship with a sister company that... with the well-known relationship of the
UK government, did the Isle of Man Government give consideration to nationalising the Isle of Man entity,
with a view to selling it on later, as was the model adopted in some cases of the UK?

100 *Mr Bell:* I do not think that was ever a serious issue under discussion.

Mr Shimmin: I think the question at that time was not to close down any options, but to have as many
options considered as possible. There was a range of options that could be considered, one of which would be
that possible scenario, but at that time we were looking to run as many scenarios as possible. So I would not
give it any extra weight above other options.

105 **Q1068. The Chairman:** I am judging the mood here, but it was one that was ruled out very early on.

110 *Mr Bell:* Sorry, perhaps I was not quite so clear. It was obviously one that was... We had to consider all
options at that point to see what the best way forward was, but I think the feeling was that, if it was possible to
get a commercial buyer expressing general interest, that would have been the best way forward. That was the
area, ultimately, that was concentrated on.

Q1069. The Chairman: Was there a feel at that time just how much that would have cost?

115 *Mr Shimmin:* I think it is fair to say that I do not think detailed costings were raised at that point. In the
circumstances we were dealing with, we were faced with the same levels of uncertainty as anybody looking at
putting together options.

120 **Q1070. The Chairman:** Were the discussions that you were having with the other banks, which were
potentially looking to take over KSF, predicated on a 100% return to the depositors or were they based on an
element of discount?

Mr Shimmin: I think, generally, an element of discount.

125 **Q1071. The Chairman:** So there was not a clear commitment at that stage for the depositors, that they

were going to get a 100% return.

130 *Mr Shimmin:* No, and I may emphasise this a number of times but, in terms of what we were dealing with at that time, there was a high degree of uncertainty and lack of definitive financial information on which both ourselves and prospective interested parties could be making decisions. So you were looking to identify, as best you could, the financial information available.

135 **Q1072. The Chairman:** In terms, then, of building a model or something to go forward with, were you constantly in touch with key creditors and representatives from the action group and such people?

Mr Shimmin: Yes, we were very conscious, and very aware, of the issues and interests of depositors and there were both direct meetings, I think, between the Minister and representatives of depositors, plus a lot of phone and e-mail contact with depositors.

140 *Mr Bell:* There was a great deal of activity round that time, particularly to do with the depositors. Naturally, they were very concerned about the plight of what had happened to the Bank. We were doing our best, on the one hand, to try and find out exactly what the situation was, to see what steps we could take to restore their fortunes.

145 Also, there was a great deal of time spent in communicating with the various depositors' groups. I have met several individuals and groups. We had almost round-the-clock e-mail and telephone contact with them, and John Spelman was one of our key advisers at the time, who met with them even more regularly, I think.

So there was a very high level of contact at the time..

150 **Q1073. The Chairman:** So are you content that you were doing what you could to manage expectations with the depositors about the recovery of their funds, in terms of timing and the amount that they were possibly likely to see back?

155 *Mr Bell:* The big difficulty we had, through all the early days, though, was that we ourselves did not have accurate information as to exactly what the value of the outcome might be and, therefore, what the potential outcome for the depositors might ultimately be. Quite understandably, I think a lot of the depositors got frustrated in some respects because they were not getting the answers they were hoping for. It was not through any lack of communication; it was just we did not have the information at that time to give.

160 **Q1074. The Chairman:** I appreciate if you have not got it, you cannot pass that on but, in terms of a liquidation, of course, 100% return is and, I think, as far as I am aware, would be, unprecedented. Was that message getting out clearly enough early on to say that there was no guarantee, other than the DCS?

165 *Mr Bell:* We could not give them any other figure in the early days because, as I say, we had no idea what that final outcome might be and I think this was probably the cause of frustration and, in some cases, anger, I think, that we were not able to give them that comfort that they could get 100% back.

The Chairman: Mr Crowe.

170 **Q1075. Mr Crowe:** Thank you, Chairman.

The Chief Minister's steering committee: can you just expand a bit on the steering committee and how often it met and who was advising you as to what was going on, because you have mentioned lack of information.

175 In the minutes, there was this HM Treasury Order, which actually restricted the amounts of information, so could you expand on the make-up of the committee, your advisers, the daily meetings and so on. Just paint a picture of the background of events at the time because we have the benefit of hindsight, where you were actually in the cauldron, shall we say, at the time – just painting a bit of a picture on that might just help the Committee.

180 *Mr Shimmin:* If I may, Chairman, if I could pick that up, the committee effectively met daily, certainly for, effectively, the first month or two of the situation. It, I think, came into being on 28th October. The committee was made up of the Chief Minister, the Treasury Minister and Mr Teare MHK. The advisers to it

were the Chief Secretary, the Attorney General and myself. We also had the Chief Executive of the FSC attending to give technical advice, as also Mr John Spelman, providing technical advice and expertise. That was the main body of the committee. We would call in people as and when thereafter.

185 Fairly early on, it became clear, as we were needing to consider in more detail our options that might be put forward, that we would need further expertise and the committee agreed to employ a firm called AlixPartners to provide the advice and expertise they brought from restructuring – so they were brought in at a relatively early stage.

190 **Q1076. The Chairman:** The UK select committee recommended that the UK and Isle of Man Governments work together to resolve the KSF (Isle of Man) issue. What approaches did the Isle of Man make to the UK government and what responses were you getting back? We are obviously talking about this period specifically after 8th October.

195 **Mr Shimmin:** The key at that point was to clarify the extent to which the UK would assist in negotiating directly with the Icelandic government.

200 **Q1077. The Chairman:** In terms of how time progressed, and how the picture cleared, you must have been looking, at the start, at scenarios anywhere between 30% and 80% to 90% recovery. When did you start getting a bit of certainty about what the recovery rate was likely to look like?

205 **Mr Shimmin:** The key problem throughout the period was the extent to which one could get certainty as to the moneys held in banks in the UK. That was an issue of regular frustration through that period, in terms of getting definitive information from the administrators in the UK. So, throughout the period, there was a difficulty in getting any further certainty around those areas. As we were able to gain information from that source, then it started to help coalesce thoughts.

210 **Q1078. The Chairman:** Are there any particular milestones in terms of obtaining a degree of certainty over things such as the Repo agreement, a minimum rate of return from the UK, in terms of knowing what you had available on the Isle of Man? Are there some key milestones there about what you knew and when?

215 **Mr Shimmin:** I think that information is reflected accurately in the minutes of the KSF Steering Group, so as that information started to become clearer it was reflected into those minutes and reflected in the work that was done with AlixPartners, but I do not think you can say, at any point, there was one digital tipping point from not having information to having information. It was a development.

The Chairman: I suppose that brings us neatly into the formulation of the scheme of arrangement, then. Mr Crowe, if you would like to...

220 **Q1079. Mr Crowe:** I think, even looking at the minutes, it was as early as 14th November 2008 that the scheme of arrangement was being considered, so it seemed to be quite an early stage that the option of a scheme arrangement was being looked at. It was a case of a rescue sale, as was at the time, or restructuring of a scheme of arrangement or liquidation. So I think it was considered at an early stage.

225 I would just like to ask for your thinking on the benefits of the scheme arrangement over liquidation, because you have talked about sale as a going concern, but there must have been this difficulty of the lack of information from KSF(UK) as to what you could actually generate. The reason for focusing on the scheme of arrangement: you might like to expand on that a bit, please, and the benefits of such a scheme.

230 **Mr Shimmin:** The reality of the situation, in terms of a liquidation, is that assets will be sold at a fire-sale type price, in all likelihood. The issues were around seeking to identify a way of getting the best return we could for the depositors etc, and one is looking at what alternatives might avoid that sort of position.

235 A scheme of arrangement, in a general concept, is one way of trying to do that and provide a more orderly result. So, at that stage, as a concept, it is very much one that needs to be borne in mind. You then start to flesh that out as to whether or not that concept can work, and that was the work that went on from that point.

Q1080. Mr Crowe: But you were hampered by the lack of knowledge of the assets of KSF(UK).

240 *Mr Shimmin:* I think all parties involved in it, whether it was looking at it from the Liquidator Provisional's point of view or ourselves, were always hampered with that.

Likewise, people who were looking to put... The advisers, in terms of getting sufficient financial information upon which to advise, had those difficulties. Those who might be interested in other alternative solutions had the difficulties of getting adequate levels of confidence in relation to the financial information. It was a fact of life at the time and one that we were not able to control.

245 **Q1081. Mr Crowe:** Did this cause difficulties when you went to court, making applications for the courts? There were, I think, three applications to court.

Was there difficulty in preparing the papers for court, shall we say, with the lack of information?

250 *Mr Shimmin:* We had to prepare on the basis of the best information we could get and, clearly, that was never as certain as we would wish it to be. So the simple answer is yes, it made it harder to do.

255 **Q1082. The Chairman:** There was, when this was all mooted, an informal committee established – referred to in the papers of the IC – which was made up of various depositors representing different groups. How many members of that committee were there?

Mr Bell: Of the Depositors' Action Group?

260 **The Chairman:** No, there was an informal committee that was established, as a consultation body, in order to get feedback. Is this something that you were aware of?

Mr Shimmin: I think we need to review the files to give you specific numbers. It is not one that I –

265 **The Chairman:** Okay. I was just looking to try and get a feel for how broad its membership was, who was invited on in order to be represented and which groups were identified. You don't –

Mr Shimmin: I would need to –

270 **Q1083. The Chairman:** One of the issues that was raised by the depositors, certainly, was the suggestion by Treasury that legal costs might be covered by Treasury – both sides' legal costs. Is this something that sounds familiar to you, in terms of the discussions that were being held with depositors?

275 *Mr Shimmin:* My recollection was that, at a later stage of the consideration of the scheme of arrangement, certain depositors were suggesting that Government should be meeting the legal costs in effectively assessing the scheme of arrangement. Is that the...

The Chairman: I was wondering if Government gave an undertaking that it would, or would consider, meeting those costs – the other side's legal costs, the depositors' legal costs.

280 *Mr Shimmin:* I think there are two elements. I think it would consider that request, because the request was made.

I think the result was that the decision was taken that Government would not meet those costs.

285 **Q1084. The Chairman:** Was that decision communicated to the depositors, inasmuch as there seemed to be an expectation, until very late in the day, that the Treasury would still be meeting their legal costs?

Mr Shimmin: My understanding is that that was communicated. I would need to check the detail about that.

290 *Mr Bell:* I think there was an element within the depositors themselves, or they were pushing constantly – *[Interruption]* – information that they were given from the Chief Minister's steering group or from the Treasury, but they felt they had a responsibility to keep pushing for this, even after the information had been given to them.

295 **Q1085. The Chairman:** In terms of the scheme of arrangement, was there, again, a suggestion from Government that if this informal committee was not on side with it, then it would not be pursued by Government, inasmuch as there would be unlikely to be a basis of support for it?

300 **Mr Shimmin:** I think the way I would refer to it is clearly, if Government was seeking to move a scheme of arrangement, if the view was taken that it felt it was unlikely to get sufficient votes in favour, then why progress it? But it is a question of identifying that view, so one was picking up a feel for what the different classes of depositors may or may not be deciding.

305 **Q1086. The Chairman:** How, then, did you go about targeting and giving information to the relevant classes to ensure that you knew, group by group, everyone was going to be on side in order to progress it, or sufficient numbers?

310 **Mr Shimmin:** There was the required information to be supplied to all creditors in relation to the court... [Interruption] supplying an explanatory memorandum, details of the calculations etc. I believe there were a series of meetings. Particularly, I think John Spelman met a number of the depositors' representative groups and sought to explain in more detail the rationale for the scheme of arrangement.

315 **Q1087. The Chairman:** One of the arguments that has been put to us is that, actually, there was one large unsecured creditor that, single-handedly, could have brought down the whole group, and it does not appear that that individual group was targeted in a way in order to ensure that they were best informed, so perhaps would you say that this was a good scheme that was marred by perhaps not doing the electoral mathematics on it?

Mr Shimmin: My view would be, no, that would be an inaccurate reflection of the situation at the time.

320 **Q1088. Mr Crowe:** Mr Chairman, can I just ask: there were three categories of creditors. Can you just expand on the three categories, please, that had to vote, and the percentage of them that was required to get the scheme of arrangement?

325 **Mr Shimmin:** There were three classes identified: a small depositor class; a large depositor class; and a non-protected class. The required voting was for 75% by value per class.

330 Overall, across the three classes, approximately 68% of all creditors voted in favour of a scheme of arrangement. The small depositor class, approximately 84% by number, representing 85% by value, voted in favour. In terms of the large depositor class, approximately 47% by number, representing 65% by value, voted in favour. In the non-protected class, approximately 93% by number, representing 9% by value, voted in favour – which is the point you are making.

Q1089. The Chairman: The requirement was to meet the target by number and by value, wasn't it, sir?

335 **Mr Bell:** Yes.

Mr Crowe: Thank you.

The Chairman: Do you want to comment, as well?

340 **Mr Houghton:** No.

Q1090. The Chairman: The Scheme of Arrangement was described by the Depositors' Action Group as 'sketchy and incomplete' and that was at a point in time on 19th February for the Court hearing.

345 However, the Depositors' Action Group, as I understand it, walked away from this informal committee in about mid January. Do you feel it was given a fair chance and a fair hearing?

Mr Bell: The Scheme itself?

The Chairman: Yes.

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Mr Shimmin: Yes.

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Mr Bell: We had several months to work with it, but we went back to the courts. The courts recognised that, on occasions, it was still work in progress and they gave us the time to actually put more detail on the Scheme to enable us to put a more detailed proposal to the depositors.

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Q1091. The Chairman: Clearly, the relationship between Treasury and the depositors has been one of growing acrimony over time. Do you feel that talks between Treasury and the depositors broke down too early on, or do you feel that there was still a good relationship in place when the Scheme of Arrangement went to the vote?

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Mr Bell: I think there was a good relationship with certain elements of the depositors all the way through this. They understood the difficult situation we were in and were very supportive, in fact, of the steps that were taken. But other elements of the depositor group clearly had different views, different priorities, and those relationships with Treasury were strained on occasions.

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Q1092. The Chairman: How were you communicating with the depositors as a group and individually? Could I just leave that as a bit of an open-ended question?

Mr Shimmin: There was a variety... There were direct discussions. The Minister met depositors. Mr Spellman met depositor representative groups.

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We were seeking to answer questions that may be supplied by e-mail or whatever. We were looking to engage and answer questions as best we could to facilitate depositors, the classes, coming to the view that they wished to do. It is putting the information, as best we can, to those people for them to make an informed judgement; not for us to make the decisions for them.

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Q1093. The Chairman: So there was a mixture of reactive communication, in terms of responding to people's e-mails and concerns, as they came in.

What was going on in terms of the proactive element and putting information out to depositors who, perhaps, were not going on the website?

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Mr Shimmin: I think we were seeking to provide the information to those who require... All depositors were provided with all the information through the Scheme of Arrangement through the court, in terms of explanatory memoranda and details. Where there were questions that may arise from that that we could respond to, we would respond to those. We would make ourselves available to answer questions, I think, through the Minister, through Mr Spelman or whoever, should those questions arise.

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Q1094. The Chairman: But you did do a fair amount of communication through that website. Did you find that a very helpful tool, in terms of collating questions and answers all in one place, in order to communicate with depositors?

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Mr Shimmin: At that stage, I think there was very... We understood the importance of trying to communicate as best we could, using whatever routes we could, with depositors and the different classes, to ensure that they could make informed judgements themselves. It was in our interests to clarify questions that they may have, so we were trying to provide that –

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Q1095. The Chairman: Do you appreciate that some depositors might have been concerned that they would have been aware, maybe – they may not have been aware – that the Bank went into provisional liquidation on 9th October whereas, if their only means of communication was written communication, in terms of letters, they would not have then heard anything until 16th December to get an initial statement, and then several months later before the Scheme of Arrangement document arrived with them? Do you think that that was adequate in terms of a communication strategy with perhaps not the majority, but certainly a minority of depositors?

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Mr Shimmin: I think our general... We were very sensitive and very aware of the need to communicate as much as possible. We were, in a variety of ways, at different times, setting up a help-desk approach and responding to e-mails, and if you will bear with me for one moment, I will give you the scale of the level of communication.

410 This is at an earlier stage and I am conscious that it refers to a slightly different situation, but in relation to the Early Payment Scheme, a help desk was working very hard to ensure enquiries were dealt with promptly. The team there dealt with more than 7,000 e-mails and letter enquiries and over 5,000 phone calls. Some depositors were making very frequent communications and requests. We were regularly posting updates on the Government website and through the Financial Supervision Commission website. Depositors were advised to check the websites of the Liquidator Provisional etc.

415 We were seeking to ensure that we could communicate as best as possible with those depositors. We were aware that there were always depositors who were concerned and wanted to be able to communicate more and differently and we tried to address those issues. So, if you are saying 'Could we have done it better?', I think we tried the best we could at that time to ensure... and we were very focused on trying to ensure that we could communicate as best we could with those depositors.

Mr Bell: I think we have just got to be a bit careful not to approach this particular issue with the benefit of hindsight. You need to understand the circumstances we were working under at the time, to try and get any information out and to get a structure in place to pass on to the depositors.

425 You also need to understand – and I am sure you do – that there was a great deal of fear among the depositors, fear of losing everything, and a number of depositors were scattered all around the world, some in quite difficult places to make contact with, as well. So there was a very volatile set of circumstances there, which put huge pressure on Treasury at the time in particular, to put this information structure together to help people.

430 **Q1096. The Chairman:** The nature of the question, of course, is that were we relying a bit too much on a reactive approach, in terms of dealing with the people who came in and were perhaps the loudest and the ones who were coming back the most, rather than going for a more organised proactive communication, ensuring that everybody was being kept informed?

435 *Mr Shimmin:* I would say that we were trying to balance both of those. Clearly, it is for the Committee to judge the extent to which we succeeded or otherwise on that. But, from our perspective, we were very aware of the need to communicate both proactively and to try and ensure that the information was available before the questions were asked, and then to respond adequately were questions asked.

440 *Mr Bell:* I think also it is worth pointing out that, whilst there were some depositors who have been very critical of the level of information they got, we had at the time some considerable number of compliments about the quality of information that was going out, as and when we got it available, so there are different perceptions of the quality of the information...

445 **Q1097. The Chairman:** There was also criticism that there was insufficient time allowed for people to consider the documents that came with the Scheme of Arrangement, make an informed decision on that, maybe take legal advice, and then communicate that back to the Isle of Man in time for the creditors' meeting. I appreciate that there are statutory timescales around this: do you think that they are adequate and do you think that, perhaps, more time should, and could, have been given?

450 *Mr Shimmin:* Ultimately, that is a view. If the views that you were expressing were accepted by the court as not having had sufficient time, then the court could define the time provided. From our perspective, I think there was adequate time provided.

455 **Q1098. The Chairman:** Perhaps straying away from the court, which would have determined whether, legally, there was enough time, and a view politically as to whether it was felt that there was sufficient time and whether, in future, that timescale may need to be lengthened?

460 *Mr Shimmin:* I think, at this stage, we believed that there was adequate time in relation to the Scheme of Arrangement provided through the necessary statutory timetables that the court required.

The Chairman: We move on to the next thing, then.

465 **Q1099. Mr Crowe:** Mr Chairman, could I just ask... Contact with Iceland during all this period: could you just expand a bit as to trying to... I think the parent guarantee. Can you just expand a bit on discussions or meetings with any of the Iceland bankers or government during this time?

470 **Mr Shimmin:** The key at the early stages was to ensure that the UK government represented the Island's interests in direct discussions with the Icelandic government: there were discussions through the period, there was a visit to Iceland – I would need to check the dates – but a visit to meet the restructuring committee in Iceland – and we knew of visits that the Liquidator Provisional was making. So those contacts we were seeking to make with the various bodies in Iceland.

475 **Q1100. Mr Crowe:** So all avenues were being explored at the time?

480 **Mr Shimmin:** Yes, and I think I would reiterate the point the Minister is making. If you look with hindsight, it is one issue, but at the time communicating with Iceland was not the easiest of situations, given the circumstances that *they* were dealing with.

Mr Bell: You also have to bear in mind the relationship between the UK authorities and Iceland at the time, which were somewhat fraught, shall we say.

485 **Mr Crowe:** Yes.

Q1101. The Chairman: I think we came to some conclusions in the first part of our remit about the suitability and ability generally of the British government to represent our interests abroad and how well they were doing that. We have seen a move on from that time of the last two years: do you believe, Minister, that with the new regime, certificates of entrustment and the way those developed, especially in more recent months, that perhaps the Isle of Man would be more empowered to take a direct stance, now, rather than the situation we were in, constitutionally, two years ago?

495 **Mr Bell:** We have certainly moved on in the last two years and I think there is a greater willingness on the part of the United Kingdom to allow the Isle of Man to carry out its own discussions. So perhaps, looking from the perspective of today, things have changed and had that situation arisen again, we may have greater freedom early on in the process to actually discuss with third parties.

The Chairman: Thank you.

500 **Q1102. Mr Houghton:** Was there an early view in Government that it wished to avoid invoking the DCS and, if so, why?

505 **Mr Shimmin:** The first thing is that it is not for Government to invoke the DCS; the DCS would be invoked through an event of default.

Mr Houghton: But the Treasury Minister would put the motion to Tynwald?

510 **Mr Shimmin:** Sorry, if I could finish the answer. Therefore, it is not for Government to invoke the DCS; it is to look at whether there are alternatives which would avoid the DCS being invoked. There is an important separation there.

Why we were looking to identify what solutions were there was set out very clearly... If you would bear with me one moment...

515 **The Chairman:** If I could just ask, Mr Shimmin, if you would not mind speaking up a bit: they are having trouble hearing you at the back.

Mr Shimmin: My apologies.

520 I think one of the points the Minister made early in this process was that Government was attempting to undertake a number of things to protect the depositors of KSF(IOM), to explore opportunities for restructuring KSF(IOM) and to make it attractive to investors, or achieve an orderly rundown to secure a good deal for creditors, whilst avoiding the triggering of an event of default that would then lead to the DCS, and to protect the Island's reputation. So at the forefront of Government's thinking was always protecting the depositors interests, but there were always also balancing these other issues as well.

525 **Q1103. Mr Houghton:** So what were the tangible benefits of the Scheme of Arrangement over the Depositors' Compensation Scheme? What was your involvement with the oversight through the period of the decision making, as to whether to invoke the DCS through Tynwald or to proceed by the Scheme of Arrangement?

530 **Mr Shimmin:** The Scheme of Arrangement was considered and moved from a conceptual stage through to the specifics through the work of the KSF steering committee. That was the body that defined and decided whether or not to take that forward. The benefits of the Scheme of Arrangement over the DCS were set out in the skeleton argument on behalf of the company and the Treasury, which was considered in the Chancery Division of the High Court on 9th April 2009.

535 So those benefits were summarised as: all creditors would receive an amount equal to the amount that they would have had, had the company been placed in liquidation; that there will be certainty as to the timing of the first three distributions in the first two years after the commencement of the Scheme; protected depositors will have certainty that they will receive the amounts which they would have received under the DCS regulations on or before the second anniversary of the Scheme becoming effective; if the total distribution paid to Scheme creditors – this was at the time – is less than 60%, all Scheme creditors will benefit because the payments that would otherwise be made to the Treasury, as assignee of the claims of protected depositors, will be available to Scheme creditors; and Scheme creditors will benefit from the Treasury's agreement to subordinate its own pre-insolvency claim.

540 So those were set out as the benefits that were seen through the Scheme of Arrangement. The Scheme of Arrangement at that time was seen by the committee as giving, in the view of the committee, a better position to the depositors than the DCS.

545 **Mr Bell:** I think there was also a thought that, under the Scheme of Arrangement, there could be a more orderly sell-off of the assets, as opposed to the potential fire sale of a DCS, which may give a higher return to the depositors.

550 **Q1104. Mr Houghton:** The Depositors' Action Group felt very strongly at the time that the primary motivation to delay in invoking the DCS, and therefore pursuing other options which bought time to develop a potential funding solution was, indeed, to protect the reputation of the Island, rather than seeking to prioritise and maximise support to the affected depositors. What was your response to that at the time?

555 **Mr Bell:** Our response was very clear. We obviously had, as paramount concern, the worry about the depositors and our desire to help them as best we could. We did, though, also have to bear in mind the reputation of the Island and, indeed, the possible financial burden which could fall on the taxpayers.

560 So we were looking at a number of areas of concern but, ultimately, as far as the Scheme of Arrangement was concerned, we believed at the time that this offered the best opportunity to help the depositors and that is why the support was there. Had we not been convinced that the Scheme of Arrangement would have been workable, I am sure we would have allowed it to go into liquidation and the DCS would have kicked in earlier.

565 **Q1105. Mr Houghton:** Thank you.

Consultation regarding the DCS had been under way in 2007 and early in 2008, yet no decisions were taken to propose an amended scheme to Tynwald at that time. Why was that?

570 **Mr Bell:** The summer of 2008, in particular – although most of 2008 – was a period of some turmoil in the banking world and, in fact, during that period, very few countries actually had a depositors' compensation scheme. Ours had been in since 1991.

So the debate about whether, in fact, a more standardised international response to depositors'

575 compensation should be developed, particularly through the European Union, was taking place during that period. Although we considered, leading up to that summer, the wisdom of taking forward an amended scheme, it was felt that it would be better, from everybody's point of view, to wait to see what evolving standards came out of Europe, as a result of the debates which were taking place elsewhere.

580 **Q1106. Mr Houghton:** Was it coincidental that high cover under the DCS was agreed on 9th October and was there adequate consultation and agreement of the amended Scheme, prior to bringing this to Tynwald?

585 **Mr Bell:** There was consultation on the Scheme. There may be criticism that it could have been more extensive, but you need to bear in mind the circumstances and conditions we were working under at that time, where the pressure was really quite intense from depositors, because of the turmoil in the banking system. Therefore, we felt it was necessary to bring forward the amendment to the Scheme when we did, in response to the external concerns which were being raised. In an ideal situation, perhaps there might have been time for wider consultation, but I think circumstances dictated we took the action that we did at the time.

590 **Q1107. Mr Houghton:** Was the Treasury satisfied, though, at that time, that it had the full legal powers to invoke the amended DCS in respect of KSF (Isle of Man)? Obviously, it had Tynwald support, but did it believe at the time it had those full legal powers in order to –

595 **Mr Shimmin:** Treasury believes, and believed at the time, that the Scheme that was in place... when an event of default occurred would trigger the Scheme in place. Therefore, an event of default had not occurred prior to 9th October, when the Scheme was approved by Tynwald. Therefore, it was clearly of the view that the Scheme approved by Tynwald would be the scheme which would govern payments should an event of default subsequently be called.

600 **Q1108. The Chairman:** Could I just ask, when the decision was taken to put... it was well documented that there was going to be a revised Scheme going to October Tynwald; obviously that was somewhat overtaken by events. When was the decision taken to recall Tynwald to put this new plan forward?

605 **Mr Shimmin:** We could look at the dates in specific terms, but it would be shortly before the request was made and notification to Tynwald Members of the recall because we had to give notice to Tynwald Members of the special sitting and then, tracking back, it was just shortly before that point.

Q1109. The Chairman: Before or after Kaupthing went to Liquidator Provisional?

610 **Mr Shimmin:** The basic issue here is: was the DCS that went to Tynwald on 9th October triggered simply by KSF? And the question is that it was not. It was triggered by the political view of the general deterioration of the economic and financial situations at that time.

615 **Q1110. Mr Houghton:** So, on gaining Tynwald approval, why did the terms of the DCS have to be amended within two weeks of the Scheme which was therefore approved? Two weeks afterwards, there was another Scheme, or an amended Scheme, in force. Why was that?

620 **Mr Bell:** I would need to review the minutes on that, but I think it was in response to some concerns which were expressed in relation to one part of the Scheme. Yes, I think I am right in saying that, because there was a limited amount of consultation: there were one or two areas which were raised after... which we believed, in hindsight at the time, were fair, and therefore we brought back a further amendment to that.

Q1111. Mr Houghton: Why was it not considered from an early stage that a financial support package could be applied to the DCS, which was a model already in place?

625 **Mr Shimmin:** The view at the time was that we should investigate a variety of options to see whether the Bank could be saved, whether an alternative solution for an orderly winding down might be a preferred solution than simply the Bank going into liquidation and the triggering of the DCS. So the preference was always to see whether, realistically, there was an option for improving the position of the depositors etc by finding an alternative solution.

630

Q1112. Mr Houghton: Moving on, then, what has been the real impact of the delays in payments out to depositors? With hindsight, could a process of earlier payments to those depositors, based on funding from Treasury, have been implemented much earlier than actually occurred?

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Mr Bell: I think Treasury worked quite swiftly to bring in early payment schemes, recognising that there were cases of hardship, particularly amongst the smaller depositors, and we wanted to do our best to help them, so I think we brought an early payment scheme forward at an appropriate time.

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Q1113. Mr Houghton: When was that Early Payment Scheme proposed? Who proposed it? What were the drivers to introduce such a scheme?

645

Mr Shimmin: I think it was something that was proposed within the KSF steering committee on or about 21st November 2008, and it was subsequently agreed by that KSF steering committee. It was subsequently approved in principle by Tynwald in December 2008.

650

Q1114. Mr Houghton: Have you the net cost to the Isle of Man Government – the net cost – of that scheme? Do you have that to hand?

Mr Shimmin: There was a report done to Tynwald which, if you bear with me, I will get the details of, which set out the position and payments of the two early payment schemes. If you bear with me for one moment, I will seek to...

Mr Houghton: Thank you.

655

The Chairman: Would you be happy for that to be followed up in writing, or do you want to hear the answer now?

Mr Houghton: I can move on, if that is what –

660

Mr Bell: I think that would be easier, Chairman, if we could find that information out.

Mr Houghton: That would be very helpful. Thanks very much indeed.

665

Mr Bell: It is on record.

Mr Shimmin: It was presented to Tynwald, so...

670

Q1115. The Chairman: Leaving aside lost interest, the figure that springs to mind was something in the region of £5 million. Is that a figure that sounds familiar to you, in terms of the overall cost of financing of the DCS?

Mr Bell: Yes, in total, our estimate at the moment, I think, is about £5 million – between £3 million and £5 million.

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Mr Shimmin: That is why I was separating the difference between... The... question was on the Early Payment Scheme. The figure that, again, will, I believe, be included within a report that is being laid before the November Tynwald, which is a half-yearly report that Treasury has done, will set out publicly the figures. Again, I can refer to those now, if you wish.

680

Mr Bell: I think, in total, Treasury released something in the region of £200 million to fund this, and it should end up with a net cost to the taxpayer of about £5 million.

Mr Houghton: Yes, it is that figure. If you could let us have that in due course.

685

Mr Shimmin: The provision made in the Government Accounts for the year ended 31st March 2010,

which is on page 40 of what is referred to as the 'Light Blue Book', was a provision of £5 million.

690 **Q1116. Mr Houghton:** And finally, Mr Bell, what process was followed whilst you were Treasury Minister regarding a review of the 2008 Depositors' Compensation Scheme?

Mr Bell: Subsequent to KSF, you mean? (**Mr Houghton:** Yes.) Once the scheme was under way, the plan... have we got time to... Yes, we started the consultation again straight away after and I reported back to Tynwald in July 2009. In fact, we can give you this timetable, if that is okay –

695 **Mr Houghton:** That would be helpful. Yes, thank you.

700 **Mr Bell:** – to show you exactly what time frame and the various steps we took during that following period. But a lot of what we were doing, as I said earlier, was really trying to reflect what was going on round about us at the time and the progress which was being made in developing the possibility of compensation schemes elsewhere, particularly looking at our competitors of the day, Jersey and Guernsey, who, when the problem arose here, did not have one. So we were watching evolving standards all round to see what would be the best structure for the Island.

705 **Q1117. Mr Houghton:** What, in your opinion, with hindsight, was the reason why it is felt that there should have been more consultation done on putting the schemes together and the reasons for the Scheme to be amended on each occasion?

710 **Mr Bell:** It was circumstances at the time that truncated the consultation. I think, given the normal course of events, we would have taken time, as Government does on consultation on matters like this. But you must always refer back to the huge pressure that we were under, during that period. It was a quite exceptional set of circumstances that came together, and that is what, in some respects, foreshortened the period of consultation that would have taken place, but it was with the express intent to make sure that the Scheme was as affordable and beneficial to depositors as we could make it.

715 **Q1118. The Chairman:** The DCS, as it stood in early October, was one that was put in place in 1991 and had only been used once. Was the committee satisfied that it was legally robust and would operate as it was expected that it would do, or was that a cause of nervousness within the steering group?

720 **Mr Bell:** I do not think there were any questions raised at all as to whether or not it would work. It had full Tynwald approval in 1991.

As you say, it had not been called on since, it had not been tested in any respect, but we were aware of the pressures that were building up to modernise the Scheme before KSF itself broke.

725 **Q1119. The Chairman:** In hindsight, perhaps, in terms of the Scheme of Arrangement, more information was coming out by the April and certainly by the final court sitting. Does Government feel that perhaps it was just too committed to the Scheme of Arrangement by that point, given that the information coming out was of a far higher rate of recovery by then? Was it felt it had to go ahead with it in order to justify the money spent on it, or is it still the view today that the Scheme of Arrangement is a missed opportunity?

730 **Mr Bell:** I think there was a robust discussion amongst the steering group at the time to assess on an ongoing basis how beneficial the SOA was and although the margins of benefit were narrowing, as greater information was coming out to us, particularly from the UK, we would not have gone back to argue the case with the court, if we had not believed that still, on balance, the SOA would have been more beneficial to the depositors. It was the depositors' interests we were concerned about at the time.

735 **Q1120. The Chairman:** On balance, it does seem to imply that it was of marginal benefit by the time it actually went forward.

740 **Mr Bell:** As you point out, Chairman, we were getting an increasing amount of information as to the developing financial health of the situation and it was certainly narrowing down the benefits but, as I say, at the end of it, we still believed collectively that that would have been the best way forward for the depositors.

745 **Q1121. The Chairman:** I think, Mr Shimmin, you mentioned earlier about a firesale that would have taken place had the DCS been called upon in October. What significant differences would you have seen between the winding down through the Scheme of Arrangement and the duty of the Liquidator to get the best value out of the assets that were there? Would it really have been that they would have had to sell everything within three to six months?

750 **Mr Shimmin:** Sorry, I do not agree with the way you have put the question. My reference to a firesale, I believe, at the start, was a fairly general comment in terms of the difference between a broad liquidation position and a broad scheme of arrangement. So in a general sense, one would expect a liquidator to have to fulfil his obligations and the general view would be that that would lead to... the assets would probably get less of a return than might be the case in another situation, as a general proposition.

755 Once we had developed beyond that, which was a general kind, into the specifics of our Scheme of Arrangement, that was worked through very much on the basis of what would be the realistic return that we could expect from that.

760 **Q1122. The Chairman:** I was perhaps seeking to test just how marginal the differences between the two... and what was seen as being the big advantage of a wind down over five years, as a wind down over a shorter period under a liquidation, and what the expectation of that was?

Mr Shimmin: The general expectation would be that a more orderly wind down will give you a better return on the assets.

765 **Q1123. The Chairman:** I was looking for something a bit more specific in terms of an amount or an estimation, or how much actually we felt that difference was going to be worth early on.

Mr Bell: The cash value you are talking about?

770 **The Chairman:** Yes.

775 **Mr Shimmin:** I do not think, at that stage... At the early stage, you are not looking or able to put a cash value on that in a general sense, other than going through the exercise and identifying what the – you used the terminology ‘a firesale’ – value might be. At the stage that we were looking at that, you were raising the concept of the Scheme of Arrangement.

Once you go beyond that and you are looking at whether the Scheme of Arrangement is a solution that is going to be beneficial, you are working up as much detail of that, but not necessarily referring it back to a direct comparison to a firesale under a figure. So the bottom line to that is I cannot give you a figure.

780 **Q1124. The Chairman:** Okay. As we understand it, the contract with AlixPartners to come up with the Scheme of Arrangement was one that was based on billed time, rather than the completion of a deliverable. Do you think that in any way hampered efforts to try and solve it more quickly?

785 **Mr Shimmin:** No, I do not think so. I think our experience was that AlixPartners were very focused on trying to deliver a solution to us in as cost-effective way as we could, and they shared the frustrations that everyone had, in terms of getting sufficient financial certainty to allow them to arrive at a recommendation.

790 **Q1125. The Chairman:** Is it fair to say that Treasury would have come out financially better off from a Scheme of Arrangement than under an immediate liquidation?

Mr Shimmin: We have not done that as a calculation to that effect, in terms of judging it. That is with hindsight, one could look back on that, but...

795 **The Chairman:** You must have had an idea of what Treasury’s recovery was, when you put this forward, though?

Mr Shimmin: In terms of... I am sorry, could you perhaps go through the question again?

800 **The Chairman:** Yes. In terms of had we pursued a liquidation either early on, or even had the Scheme of Arrangement been passed in... Perhaps the April is the best place to differentiate this. If it came down to there is the Scheme of Arrangement being put forward by the Isle of Man Government in April, and there is the liquidation, which is the alternative, which one was it felt that the Isle of Man Treasury would come out better from?

805 **Mr Shimmin:** I think, at the time, the question would be that one could have more certainty as to the figures on the DCS, but that the view remained that, overall, the Scheme of Arrangement was viewed as the preferred solution. In terms of, at April, doing a figure exercise to quantify that in the way you are putting forward was not –

810 **Q1126. The Chairman:** You had not assessed as far as Treasury was concerned, which one would have been better for Treasury?

815 **Mr Bell:** If you are suggesting that we supported the Scheme of Arrangement just because it was financially better for Treasury, that was not the concern.

Q1127. The Chairman: I am just asking the question, which one was better, but you do not have that assessment. Okay.

820 It is also fair to say that, as time has proceeded, and as the recovery rate has risen, that has been a major undermining factor for the Scheme of Arrangement. So, as more information has come out, as the recovery rate has risen, the Scheme of Arrangement's attractiveness has declined.

Mr Shimmin: With hindsight and 20:20 vision, one would accept that. Would that have changed the situation at the time? I do not think... We did not have the benefit of that hindsight.

825 **Mr Bell:** I have to stress just how difficult it was to get accurate information at that time, to make a value judgement. As Mr Shimmin says, it is easy, now today, to sit back and look back and say we would have been better doing one course than another. It was, right across the board, very, very difficult to get any information out to put a fair structure on any of these schemes, so that we could actually be 100% confident about them.

830 **Q1128. The Chairman:** I do not think there is any doubt that that was certainly the case in October 2008; perhaps the question is how near to that tipping point we were in April 2009, when the Scheme was put to the court.

Mr Shimmin: It is a general statement.

835 The factors that Treasury was taking into account were not... To respond to your question directly, presumably Treasury would have been criticised, equally, had it simply taken a decision purely on the basis of the consideration of the taxpayer implications, at that stage. I go back to the general point, that Treasury was looking to balance all the interests of all the parties in arriving at a solution at that point.

840 **Q1129. Mr Crowe:** What you are saying, then, is you wanted to ensure that you had the greatest realisation of assets when you were looking at the whole situation, so you were trying to get the best deal, shall we say, for the depositors and creditors?

845 **Mr Shimmin:** That was always at the heart of what Treasury and the... *[Interruption]* committee of KSF was trying to achieve.

Q1130. The Chairman: We have talked a lot about the Depositors' Compensation Scheme. In reality, this is a Scheme that does not provide compensation; it provides a guarantee. Is it perhaps fairer to call this a depositors' guarantee scheme, rather than a Depositors' Compensation Scheme?

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Mr Shimmin: I do not think so. I think the terminology is adequate.

Q1131. The Chairman: You do not think it gives rise to concerns about actually being able to receive

855 compensation in terms of other losses, other than immediately what was lost and what is therefore guaranteed?

Mr Shimmin: It seems to me it is a terminology that has been in use for a period of time and, broadly, is understood and accepted. One can always change terminology. I do not believe that the terminology is creating a problem that needs to be solved.
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Q1132. The Chairman: One of the matters that was put to us in the DAG submission was that they felt that Treasury were promoting the interests of local depositors over others. Can you think of any reason why they would think that?

865 *Mr Bell:* None whatsoever. Treasury have been very fair, I think, in trying to recognise the rights of all depositors.

Q1133. The Chairman: Did you find, as you were weighing up the differences between the liquidation argument and the Scheme of Arrangement, that there were hurdles and problems, in terms of our Manx insolvency law, that made either one of them difficult to pursue?
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Mr Bell: I think there is certainly a recognition that Manx insolvency law needs modernising. That has been recognised for quite some time, but whether it caused a particular problem in our discussions... I do not recall it having been raised as a problem.
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Mr Shimmin: Likewise, I do not recall it being raised as a specific problem in this context.

Q1134. The Chairman: One of the other scenarios for the Depositors' Compensation Scheme, going forward, is that it be pre-funded. What is, was, the view from Treasury on that?
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Mr Bell: It is an issue which certainly has been debated, and so far has been not deemed to have enough support to take it forward. In future discussions, that may well be something which will be on the agenda.

885 *Mr Shimmin:* I would simply say, Tynwald has approved the Scheme as it is very recently. That Scheme is one that we would accept introduces greater flexibility which could provide means of front-ending money into the Scheme to assist payments to depositors earlier. Pre-funding is only one possible solution in that route.

890 *Mr Bell:* Any move in that area, of course, would also reflect on what international standards towards these types of schemes might consist of, and what competitor jurisdictions might do.

Q1135. The Chairman: The Depositors' Compensation Scheme and the actions taken in respect of KSF are very specific to one situation. They represent a mid-tier bank on the Isle of Man.

895 In terms of a large-scale bank, if anything happened there, would you still feel the DCS is fit for purpose or do we need a more graduated approach to –

Mr Shimmin: I think the view we take is that the Scheme, as put to Tynwald most recently, is fit for the purpose.

900 **Q1136. The Chairman:** I suppose, really, that just brings me to lessons learned and what would you do differently, if this ever happened again in the future?

905 *Mr Bell:* That is a good question. I think, given the frenetic conditions at the time, Treasury and the Isle of Man Government performed an honourable option to try and help the depositors. Whether we would have done it any differently, looking back, it is difficult to say. I cannot really reflect on that at the moment.

Mr Shimmin: I think we have tried to learn lessons, particularly in relation to some of the changes introduced into the latest Depositors' Compensation Scheme. I think we would need to consider the extent to which we have a greater co-ordination of communication, if that is possible, between the different parties, for

910 looking at the practical lessons in that context.

The Chairman: Anything?

915 **Mr Houghton:** No, thank you.

The Chairman: Last chance. Alan?

Mr Crowe: No, thank you, Chairman.

920 **The Chairman:** Roger?

The Clerk: No, thank you.

925 **The Chairman:** In which case, thank you very much for appearing before us this morning.

Mr Bell: Thank you, Chairman, and apologies again for the state of my health.

Mr Shimmin: I will submit those requested papers to you.

930 **The Chairman:** Thank you very much.

The Committee sat in private at 11.46 a.m.