

STROUD DISTRICT COUNCIL

**AGENDA
ITEM NO**

CABINET

10 JUNE 2010

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Report Title	COUNCIL DEPOSITS WITH THE ICELANDIC BANK, GLITNIR
Purpose of Report	To inform Members of the current position regarding the Council's deposits with Glitnir Bank, the process for recovery and the legal implications of that process. It also explains the accounting treatment required for the Icelandic deposits in the 2009/10 accounts and seeks approval to carry forward budget for costs associated with defending our case to be treated as preferential creditors in the High Court.
Decision(s)	Cabinet RESOLVES: <ul style="list-style-type: none"> a) to note the current position and the legal and financial implications; b) to agree that the LGA should continue to act as agent for the Council in this matter and that the Council should participate in the group claims for recovery of its deposits as priority claims through the Icelandic Courts; c) to agree that the Head of Finance, in consultation with the Cabinet Member for Finance and the Head of Legal Services take all necessary steps to participate in and progress the group claims to maximise the Council's potential for recovery of its deposits; d) that the impairment for 2009/10 is capitalised and MRP is charged as set out in paragraph 22; e) that £40,000 is carried forward from the provision to meet legal costs in 2010/11.
Consultation and Feedback	None
Financial Implications & Risk Assessment	Regulations require that the deposits at risk in Iceland are accounted for as losses in the Statement of Accounts for 2009/10. As such, £2.69m has been 'impaired' or written off, of which £2.25m has been capitalised using the Capitalisation Direction agreed by the Government. The difference of £19,000 will be a charge on the revenue account in 2009/10. By using this direction, the Council will have to make a Minimum Revenue Provision (MRP) charge to the General Fund of £42,000 each year for 20 years from 2010/11.

<p>Financial Implications & Risk Assessment Cont'd/...</p>	<p>This is purely an accounting requirement and does not mean that the deposits are lost. Should the deposits be repaid, the accounting entries would be reversed and the MRP would not need to be charged. If they are lost, the MRP will be a real cost to the revenue account for 20 years and will need to be included in the Council's annual budget.</p> <p>There is budget provision of £50k for costs arising in the process of recovering the deposits. Costs to date are £8,466. The costs for taking the case to the High Court are estimated to be between £15-20k and this could more than double if the case is lost. It is recommended that £40,000 is carried forward from the provision made in 09/10 to 2010/11 to cover potential costs arising. The risk of losing the deposits remains although the impact of such a loss is reduced by the capitalisation directive.</p> <p>Sandra Cowley, Head of Finance Tel: 01453 754136 Email: sandra.cowley@stroud.gov.uk</p>
<p>Legal Implications</p>	<p>In October 2008, the Icelandic Government introduced and passed the "Emergency Act ". This Act elevated local authority deposits in the Icelandic Banks from general unsecured status to rank as alongside other preferential claims.</p> <p>In December 2009, the winding up board of Glitnir Bank determined that all local authority deposits in Glitnir will be treated as unsecured creditors. It is this decision amongst other things that is being challenged in the Court.</p> <p>If the Icelandic Court decide that all we are unsecured creditors rather than preferential creditors, the local authorities will rank as ordinary Creditors and therefore, we may not be able to recover the full amount invested. Local Authority cases are expected to be referred to court shortly. A number of authorities have been selected by the winding-up board as "Test Cases" to allow the full range of issues to be argued before the Icelandic Courts. These judgements will not be automatically binding on other cases. Therefore, to ensure the earliest possible resolution of matters for all authorities, the winding up board has been invited to refer all authorities' claims to court now. The Court processes in Iceland are likely to take around 12 months. Distributions to creditors will not be made until the Court has made a final decision.</p> <p>The process of recovery entails the following main stages: references to the Icelandic District Court of issues in dispute, consideration and determination by the Icelandic District Court, possible lodging of or responding to appeal(s) in the Icelandic Supreme Court, subsequent distributions to creditors by the winding up board as part of the formal winding up process (this will be either as a general unsecured or priority creditor)</p> <p>Whilst it is too early to assess when the matter will come</p>

	<p>to trial and how long the trial is likely to last, it is unlikely to occur before November 2010. Judgement will be delivered within four weeks thereafter.</p> <p>Each party will have two weeks from the judgment to appeal the decision to the Icelandic Supreme Court. It is too early to assess the merits, process and timescales for an appeal.</p> <p>It would be both pre-mature and potentially damaging to the final outcome of this case for Cabinet to discuss legal issues or consequences relating to this complex litigation. The only matter Cabinet should address at the present time is whether to resolve to support the current group action, to maximise the chances of recovery.</p> <p>Bhavna Patel, Head of Legal Services Tel: 01453 754369 Email: bhavna.patel@stroud.gov.uk</p>
Report Author	<p>Sandra Cowley, Head of Finance Tel: 01453 754136 Email: sandra.cowley@stroud.gov.uk</p>
Portfolio Holder	<p>Councillor Nigel Cooper, Cabinet Member for Finance Tel: 01452 813870 Email: cllr.nigel.cooper@stroud.gov.uk</p>
Options	<ul style="list-style-type: none"> ▪ The impairment required in the accounts for 2009/10 could be financed from the Council's revenue resources; however, this would put considerable pressure on the Council's reserves and balances which would have to be re-instated over a much shorter period. ▪ The Council could accept the WUBs decision which means accepting that claims are general unsecured claims and forego the claim for interest and costs. This would reduce potential recoveries by approximately 70%.
Performance Management Follow Up	<p>Members will be kept informed of any developments with the Court action being taken.</p>
Background Papers	<p>LGA briefing notes and correspondence from Bevan Brittan CIPFA LAAP Bulletin 82</p>

Background

1. During 2008/09, the Council placed 2 deposits totalling £3 million in the Icelandic Bank, Glitnir. The bank went into administration in October 2008 and to date the two deposits have not been repaid.
2. There were 127 local authorities nationally with a total of £954 million invested in Icelandic banks at the time the banks went into administration. As a result the Local Government Association (LGA) took on the case and has been representing all the Councils at meetings with the banks and lobbying the Government to secure the best outcome possible.
3. Each of the Icelandic Banks is in a different situation and so the process for recovery of the deposits varies depending on where the deposits are held. In the case of Glitnir, the Emergency legislation in Iceland at the time of the banks' collapse, elevated the Council's deposits to priority claims and as such, 100% of the deposits plus the interest would be recoverable.

4. The Council, through Bevan Brittan, lodged its claim in the insolvency claiming depositor priority for the outstanding deposit, penalty interest and costs. However, the Winding Up Board (WUB) rejected the Council's claim for priority. It accepted the principal amount claimed as a general unsecured claim and rejected the claim for interest and costs. It is worth noting that the WUB for Landsbanki accepted the principal amount of the Council's claims as a priority claim and so the two WUBs are in conflict.
5. Bevan Brittan, on the Council's behalf filed formal objections to the WUBs decision in accordance with Icelandic procedure. Mediations took place in February to attempt to resolve the issues in dispute. These were unsuccessful and the WUBs for both Landsbanki and Glitnir selected test cases from within the wholesale depositor group which have now referred the matter to the Icelandic District Court to resolve. Stroud is not one of the test cases.
6. All Councils represented by the LGA, Bevan Brittan, Logos (Icelandic Counsel) and UK specialist counsel, agreed to share costs incurred in progressing the recovery of the Icelandic deposits in proportion to the value of their deposits. To date, Stroud's share of the costs incurred amount to £8,466.

Current position and the litigation process

7. The twelve test case claims were referred to the District Court in April and the WUB is still considering whether to refer the remaining non-test case claims to court.
8. At this stage, all Councils need to confirm that Bevan Brittan are instructed to represent them in the Icelandic proceedings to secure a decision as to whether or not the wholesale deposit claims are entitled to priority under the Icelandic insolvency regime.
9. Bevan Brittan has provided the Council with the estimated cost of taking the case through the High Court. For Stroud, the cost is estimated to be between £15,000 and £20,000 and will be higher if the appeal is lost. In the event the appeal is lost, the Council will then need to decide whether it wishes to pursue the case through the Supreme Court.
10. Under Article 16 of the Constitution, the Head of Legal Services is authorised to institute, defend or participate in any legal proceedings in any case where the Head of Legal Services considers that such action is necessary to protect the Council's interests and is satisfied as to the available evidence. The Head of Legal Services, in consultation with the Head of Finance, the Chief Executive and the Cabinet Member for Finance agreed to instruct Bevan Brittan to continue to act on our behalf in the litigation process.
11. The Head of Finance has made it clear to Bevan Brittan that the consent is based on the information currently available and in the event that legal costs vary from that currently estimated, further approval would be needed.
12. Initial hearings will take place in May/June 2010, when preliminary matters will be considered and a timetable will be set for the filing of written submissions. Once submissions are filed there will then be a review hearing at which further directions will be considered and the trial date set.
13. Whilst it is too early to assess when the matter will come to trial and how long the trial may last, it is unlikely to occur before November 2010. Judgement will be delivered within four weeks of the trial closing.
14. Each party will have two weeks from the date of the judgement to appeal the decision to the Supreme Court. It is too early to assess the merits, process and timescale for an appeal.

15. Bevan Brittan and Logos will be providing advice on merits once the written submissions have been filed. Either the way, it is in the Council's best interests to participate in the litigation. If it does not do so it will need to withdraw its objection and accept the decision of the WUB which for Glitnir means accepting that claims are general unsecured claims and forego the claim for interest and costs. This would reduce potential recoveries by approximately 70%.

Accounting Regulations for 2009/10

16. When the accounts were closed in 2008/09, the Government passed legislation which allowed Councils to defer accounting for any losses due to the uncertainty surrounding the potential for recovering losses.
17. For 2009/10, the Government has not permitted the deferment to be extended and so Councils will have to 'impair' or write-off the potential loss based on the estimated value of the banks assets known at the time of closing the accounts. For Stroud, this is currently estimated to be £2.269 million.
18. The Government did allow Councils to apply for a 'capitalisation directive' which permits the Council to treat the write-off as capital expenditure and spread the cost over 20 years. Stroud's application for £2.25 million was successful. The difference between the impaired amount and the amount capitalised is £19,000 and will be charged to the General Fund revenue account in 2009/10.
19. Had the Council's application not been successful, the full amount of the impairment would have to be met from the Council's revenue resources i.e. temporary borrowing from General Fund balances and earmarked reserves. The advantage of using the capitalisation directive is that the impact on the Council's revenue resources is significantly reduced in the short term as the cost can be spread over a number of years.

Minimum Revenue Provision (MRP)

20. Local authorities are required by Statute and associated Statutory Instruments to charge to the revenue account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the revenue account was referred to as the Minimum Revenue Provision (MRP). The Council has to set an MRP Policy annually and this has to be approved by Council before the start of the financial year.
21. In the Treasury Management Strategy, Annual Investment Strategy and MRP Strategy 2010/11 report to Council on 21 January 2010, the MRP Policy Statement 2010/11 says:

'As the Council has a negative Capital Financing Requirement (CFR) and is currently debt free there is no requirement to charge MRP. As long as this position is maintained no MRP will be charged. If the CFR becomes positive in future years it is proposed to charge MRP to revenue based on the Asset Life Method by equal annual instalments.'
22. By using the Capitalisation Direction referred to above, the Council's CFR will become positive and so the Council will have to charge MRP on the positive amount. The CFR will change from -£1.418m to £0.832m therefore the MRP will be approximately £42,000 per annum for 20 years and would be charged to revenue from 2010/11.
23. In the event that the deposits are recovered in 2010/11, the CFR would be reduced again and the MRP would not need to be charged. However, if the deposits are lost, the MRP of £42,000 will be a real cost to the revenue account for 20 years and will need to be included in the Council's annual budget.

24. The Capital Financing Requirement reflects the Council's borrowing need. If the CFR is £832,000 this means the Council could borrow this amount if necessary to keep balances intact. Advice is currently being sought from Sector on the most appropriate course of action.
25. It should be noted that this is a temporary financing arrangement until such time as the outcome of the court case is known. Based on information provided by Bevan Brittan and the LGA, a High Court decision is possible by December this year.