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<b>Committee:</b>	<b>Council</b>	<b>Agenda Item</b>
<b>Date:</b>	<b>21<sup>st</sup> October 2008</b>	<b>9</b>
<b>Title:</b>	<b>Financial Markets and Investment Income</b>	
<b>Author:</b>	<b>Adrian Webb, Interim Director of Central Services. 01799 510421</b>	Item for Decision

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## 1. Summary

- The Council has an investment with Landsbanki Islands hf of £2.2m.
- This investment was for a period of 364 days, and due for repayment on Wednesday, 15<sup>th</sup> October 2008.
- Landsbanki was put into receivership by the Icelandic government last Tuesday, 7<sup>th</sup> October 2008.
- At the time of writing this report officers have no information as to whether this investment will be repaid, and whether the interest due of nearly £135k will also be paid.
- Guarantees have been given by the UK government that all retail deposits will be refunded with the first 20,000 euros in each case from the Icelandic government.
- The Council's £2.2m is classed as a commercial investment for which, to date, no guarantees have been given. Treasury officials from the United Kingdom government are currently in urgent discussions with officials from the Icelandic government to resolve the issue.
- Latest estimates indicate that at least 100 local authorities in England, Scotland and Wales have investments, totalling at least £850m in collapsed Icelandic banks. In addition there are a number of police authorities, charities, and other public bodies with investments in Icelandic banks.

## 2. Recommendations

- Members request officers to provide updates on the progress in trying to recover the principal and interest via the Members Bulletin, and through a formal report to Finance and Administration Committee in November 2008.
- Officers to prepare the 2008/09 revised budget on the assumption that an estimated £200,000 of investment interest will be lost in the current financial year.
- Officers monitor the situation in the period up to setting the Council Tax in February 2009, with a potential loss of an additional £140k income in 2009/10 also to be absorbed.

- Members note the potential problems for the Essex County Pension Fund in the current financial market, and the impact on the Council's future budgets.

### 3. Background Papers

- Treasury Management Strategy 2008/09. Council 19<sup>th</sup> February 2008.
- Treasury Outturn 2007/08 report Finance and Administration Committee, 25<sup>th</sup> September 2008.

### 4. Impact

Communication/Consultation	There are no specific Communication/Consultation implications in this report.
Community Safety	There are no specific Community Safety implications in this report.
Equalities	There are no specific Equalities implications in this report.
Finance	There will be a significant adverse impact on the General Fund revenue budget for 2008/09 of around £200k from lost interest income. In addition there may be a further loss of £140k investment income in 2009/10 if the principal is not returned before the end of March 2009. In addition the Council may possibly also lose the original £2.2m investment which will have to be found from other sources if there is no resolution to talks between the British and Icelandic governments.
Human Rights	There are no specific Human Rights implications in this report.
Legal implications	The Icelandic Financial Services Authority has taken over the powers invested in Landsbanki's shareholders and Directors. A receivership committee has been appointed which has assumed the role of the Board of Directors. The objective of the committee is to ensure the continuing operations of the commercial banking operations of Landsbanki Islands hf. in Iceland.
Sustainability	There are no specific Sustainability implications in this report.
Ward-specific impacts	There are no specific Ward-specific implications in this report.
Workforce/Workplace	All staff have been advised by the Chief Executive of the

	Council's current position with regard to this investment.
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## 5. Situation

### The Council and the money market

1. Throughout the financial year the Council has available to it monies to invest in the money markets. These funds come from advance receipts from council tax and business rates, Housing benefit subsidy, Rents, S106 funds, PFI Reserve, and the General Fund Balance.
2. The timing of a large proportion of receipts is such that monies are received in advance and in respect of Council Tax, for example, this is then paid over to the County Council, Police and Fire authorities in 12 monthly instalments each year.
3. The Council invests available money in accordance with the Treasury Management Strategy which was approved by Council on 19<sup>th</sup> February 2008 (minute C86 refers).
4. The Council's Treasury Management Strategy meets the requirements of both the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. The Council is required to comply with both codes through regulations issued under the Local Government Act 2003.
5. Within the Council's Treasury Strategy all monies available for investment are combined for placing in the money market so for example, council tax receipts are not kept separate from business rates or rents or reserves.
6. The Council employs Butlers as its treasury management advisors. Butlers is a consultancy company specialising in treasury advice to the public sector, and is part of ICAP Group, a leading financial broking organisation. Butlers provides the Council with:
  - Weekly updates on the current week's financial market activities and the following week's expected events,
  - Monthly reports on capital accounting issues,
  - Monthly reports on credit ratings for the Council's agreed treasury institutions,
  - Immediate updates on changes to credit ratings of approved investment institutions,
  - Spring and Autumn seminars on financial matters relating to treasury management,
  - Periodical on-site visits to review treasury policy.

7. A review of the performance of the Treasury Management function for 2007/08 was reported to Finance and Administration Committee on 25<sup>th</sup> September 2008 (minute FA 17 refers).

#### **Landsbanki Islands hf**

8. The only money the Council currently has invested outside of the British Isles is £2.2m with Landsbanki Islands hf.
  - This investment was initially for a period of 364 days from 18<sup>th</sup> October 2006.
  - The investment was renewed for a further period of 364 days on 17<sup>th</sup> October 2007, and was due for repayment on Wednesday, 15<sup>th</sup> October 2008.
  - Landsbanki was put into receivership by the Icelandic government last Tuesday, 7<sup>th</sup> October 2008.
  - At the time of writing this report officers have no information as to whether this investment will be repaid, and whether the interest due of nearly £135k will also be paid.
9. At the time of re-investing with Landsbanki in October 2007 the short term credit ratings (investments up to a year) for Landsbanki, provided by our financial advisors, for the three major credit rating agencies were as follows:
  - Fitch Short Term F1
  - Moody's Short Term P1
  - Standard and Poors Short Term No rating

The Council's policy is to lend for periods of less than 365 days to institutions with a minimum Fitch credit rating of F1. For members information, at no time over the last 2 years has there been a Standard and Poors credit rating for Landsbanki.

10. Apart from a 5 week period in April and May 2008, when on negative watch (rating under review, not down-grading), the rating for Landsbanki only went below our investing minimum rating for the first and only time on 30<sup>th</sup> September 2008. Officers spoke immediately with the investment brokers who assured the Council that the money was safe, and, in any case as it was a fixed term deposit the Council had no opportunity to withdraw the funds early.
11. Had the money been repaid to the Council on 15 October the principal would have been re-invested in the money markets and would have gained, at current rates, a further estimated £65k of interest in 2008/09. In effect this means that the Council has a potential loss of interest against budget of £200k in the current financial year.

12. The Council's General Fund budget for 2008/09 for Investment Income is £377,530, which is a substantial sum for supporting the Council Tax. A loss of around £200k from the non-return of the Landsbanki investment together with its reinvestment from 15<sup>th</sup> October 2008 removes over half of the investment income budget for 2008/09.
13. It is possible that the negotiations to recover the principal sum from Iceland will be lengthy. If the Council does not recover the money before the end of February 2009 it is likely it will need to borrow to meet payment demands on the Council during March 2009. This will incur interest charges for which there is no budget, and this will further reduce the Council's investment income.
14. Landsbanki is in receivership. An administrator can be called in before a company is placed in receivership with the aim of saving it and getting it trading again. If this cannot be achieved it falls to them to secure the best deal for all creditors involved before the company is wound up. The order for paying out of creditors should that be necessary is as follows:
  - Preferential creditors - such as the bank and employees
  - Secured creditors - lenders that have money lent to the business against secured assets
  - Other creditors - the council falls within this category

There is at present no indication of how many creditors or the value of their investment is in the first two categories.

15. The Council will need to consider how the loss of the £2.2m can be replaced if/when it becomes clear that the Council is not going to be repaid its investment.

### **Other Investments**

16. Attached as Appendix One is a list of the Council's investments as at 13 October 2008. This shows that the Council had 12 external fixed term investments totalling £14.6m of which only 1 (£2.2m with Landsbanki), is outside the British Isles. For members information, at a comparable date last year, (30<sup>th</sup> September 2007), the Council had 4 fixed term investments totalling £7.4m (£3.4m with Landsbanki), of which all but £1m were with Icelandic banks.
17. Council officers have been reacting to recent market fluctuations by reducing the amount invested with any one organisation, spreading the risk and generally this has led to investing smaller fixed term deposits in more building societies. Although investment interest rates may not be as high with such institutions the main aim is to minimise risk to the principal investment.

18. The monies invested with Allied Irish Bank are in a deposit account and funds are available for deposit or withdrawal without any notice period. The Irish Government has guaranteed all deposits in Irish banks until 2010.

19. The Bank of Scotland Corporate Base Plus Account is also a deposit account but any withdrawal is subject to 7 days notice. The Government announced on 13<sup>th</sup> October that taxpayers are investing up to £31.5bn in Royal Bank of Scotland (RBS) and Halifax Bank of Scotland (HBOS). In addition Lloyds TSB is in the process of buying HBOS.

### Government Assistance

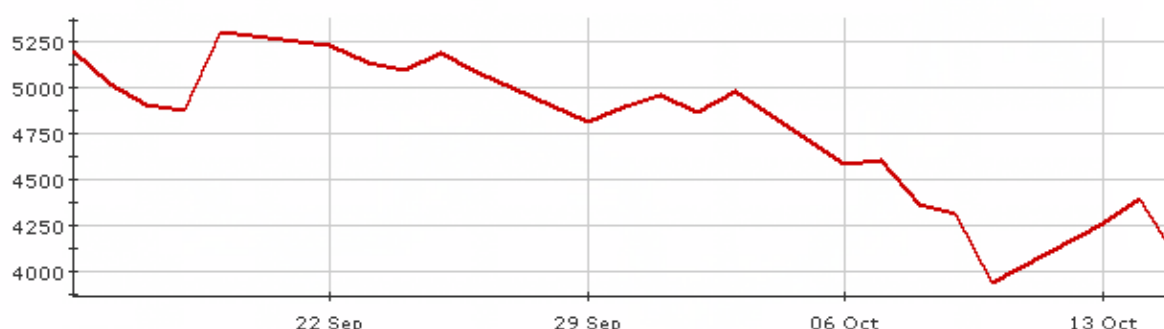
20. It was announced on 15<sup>th</sup> October 2008 that this Council was one of three that would be receiving early assistance from a team of financial experts. The team will be arriving on the 17<sup>th</sup> October to offer advice and guidance. A verbal update will be given at the meeting on the outcome of this visit.

### Essex Pension Fund

21. Within the Medium Term Financial Strategy Update reported to Finance and Administration Committee on September 25<sup>th</sup>, it was highlighted that the recent pressures on the Stock Market and the worldwide credit crunch may impact on Council's pension contribution budgets from 2011/ 12 onwards.

22. Uttlesford is a member of the Essex Pension Fund. A large proportion of pension contributions from staff and local authorities paid in to the Fund are invested in shares to provide sufficient revenue to pay the retirement pensions of former employees.

23. Share prices have dropped dramatically over the last month which has the effect of potentially significantly reducing the long term value of the Pension Fund. In mid September the FTSE 100 stood at 5,300 but by 15<sup>th</sup> October that had dropped to 4,079.



24. The next review of the Essex Pension Fund by the Actuary is due in late 2010, and if the market fails to recover quickly, it is possible that the Council's contribution to the fund will have to increase significantly in 2011/12,

impacting directly on the Council's General Fund and Housing Revenue Account budgets.

25. When the Medium Term Financial Strategy (MTFS) for the period 2009/10 to 2011/12 is submitted to members for approval in February 2009, the new Year 3 of the MTFS will have to reflect potential pressures on this Council's contributions to the Essex Pension Fund.

### Risk Analysis

Risk	Likelihood	Impact	Mitigating actions
The Council does not receive its investment of £2.2m back from Landsbanki Islands hf.	4	4	Treasury officials are still in discussions with Icelandic government officials.  The Local Government Association is holding talks with the government about assisting local authorities.  The Council will have to determine how it is going to replace the lost £2.2m investment of its reserves and balance.
The Council does not receive payment of the £135k interest on the investment.	4	4	There is a risk of reductions in services being required in order to balance the 2008/09 budget.
There is a possibility that the Council may lose up to £140k in investment income in 2009/10 if the Council does not receive the £2.2m investment by 31 <sup>st</sup> March 2009.	4	4	There is a risk of reductions in services being required in order to balance the 2009/10 budget.

1 = Little or no risk or impact

2 = Some risk or impact – action may be necessary.

3 = Significant risk or impact – action required

4 = Near certainty of risk occurring, catastrophic effect or failure of project.

Financial Markets and Investment Income  
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## Appendix One

FIXED TERM DEPOSITS				Fitch Ratings (deal date)					
				Short	Long	Support			
			UDC Minimum requirement - Fitch	F1	AA-	3			
			UDC Minimum requirement - Moodys	P1	AA3	n/a	£		Rate
17-Oct-07	124	Prebon	Landsbanki Islands HF	F1	A	2	2,200,000	Fixed to 15/10/08	6.15000%
01-Jul-08	149	Sterling	West Bromwich Building Society	F1	A	3	1,800,000	Fixed to 19/11/08	6.06000%
15-Jul-08	151	Icap	Chelsea Building Society	F1	A	3	1,200,000	Fixed to 18/12/08	5.97000%
01-Aug-08	152	Prebon	Chelsea Building Society	F1	A	3	1,000,000	Fixed to 18/12/08	5.88000%
01-Sep-08	155	Sterling	Norwich & Peterborough B.S.	P1	A2	n/a	1,000,000	Fixed to 18/02/09	5.98000%
01-Sep-08	156	Prebon	E.B.S. Building Society	F1	A	3	1,000,000	Fixed to 18/02/09	5.94000%
25-Sep-08	159	Sterling	Principality Building Society	F1	A-	3	1,000,000	Fixed to 19/03/09	6.25000%
01-Oct-08	160	Sterling	E.B.S. Building Society	F1	A	3	1,000,000	Fixed to 22/01/09	6.37000%
01-Oct-08	161	Sterling	Norwich & Peterborough B.S.	P1	A2	n/a	1,000,000	Fixed to 02/03/09	6.35000%
01-Oct-08	162	Prebon	Britannia Building Society	F1	A	3	1,000,000	Fixed to 23/02/09	6.26000%
02-Oct-08	163	Prebon	Coventry Building Society	F1	A	3	1,000,000	Fixed to 22/10/08	5.40000%
10-Oct-08	164	n/a	Barclays Bank	F1+	AA	1	1,400,000	Fixed to 17/10/08	4.55000%
<b>Total Fixed Term Deposits</b>							<b>14,600,000</b>		

SHORT TERM BANK INVESTMENTS	£	Rate	Account Type
Allied Irish Bank (Gb) Treasury Account	1,821,668.07	5.15%	Instant Access
Abbey National Business Reserve	65.62	3.20%	Instant Access
Bank Of Scotland Corporate Base Plus Account	1,971,076.17	6.13%	7 Day Notice
	<b>3,792,809.86</b>		

Total Invested as at 13 October 2008 - £18,392,809.86