By: John Simmonds, Cabinet Member - Finance
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To: Cabinet – 30 November 2009

Subject: **UPDATE ON ICELANDIC DEPOSITS**

Classification: Unrestricted

Summary: To update Members on progress on recovering the Icelandic deposits.

FOR INFORMATION

INTRODUCTION

1. This report is to update on progress made on recovering money deposited in 3 Icelandic owned banks.

2. The total exposure was £50.35m, £18m in Heritable a UK domiciled and regulated bank, £15m in Glitnir and £17m in Landsbanki. Of this £33m relates to KCC, £16m to the Pension Fund and £1m to Fire.

3. Since October 2008 KCC has played a lead role in the recovery process. KCC's Head of Financial Services is one of two local authority representatives on the Heritable Creditors Committee and is also the local authority representative on the Glitnir Informal Creditors Committee and the Landsbanki Informal Creditors Committee. The proceedings at these meetings are governed by tight confidentiality agreements and information gathered at them cannot be shared in a public report.

4. The Local Government Association has coordinated the response across the local authorities with deposits and KCC is represented on the overall Steering Committee and the Glitnir / Landsbanki Committee. The latest LGA briefing is attached in the Appendix.

5. Through the LGA the Steering Committee commissioned Bevan Brittan to provide legal advice and Ernst & Young financial advice. This work has been of the highest quality. Costs are shared on an equitable basis and are managed through the overall Steering Committee.

FINANCIAL ENVIRONMENT

6. The failure of the Icelandic banks was an event directly linked to the near collapse of the worlds banking sector in October 2008. It is now clear that without what was effectively the nationalisation of Royal Bank of Scotland and Lloyds Banking group their position would have been no different to the Icelandic Banks.

7. The LGA has published information showing 125 English local authorities with a total deposits of £932.2m in the Icelandic banks split 39% Landsbanki, 29% Heritable, 20% Glitnir and 12% KSF. In addition there are a number of Scottish and Welsh authorities, Police Authorities, Transport for London and of course the Audit Commission with deposits. There are also a wide range of organisations in the corporate sector were exposed but they have been less open about their exposure, it is estimated that the exposure of Western banks is in the region of €60bn.

8. The total KCC deposits as at 8 October 2008 was as high as £460m and diversified across 31 institutions in part due to a defensive position taken up by the Kent Pension Fund. From September 2007 the Superannuation Fund Committee moved out of risky assets and held Cash reaching a peak of £160m. This action saved the Pension Fund at least £40m. In late 2008 the Pension Fund started to reinvest Cash into equities and this move was well timed. The Pension Fund has increased in value by £500m from 1 April to 30 September as equity markets recovered.

9. With the benefit of hindsight one year on it is clear that the exposure to loss on the Icelandic deposits is directly the result of an unprecedented global financial crisis which has resulted in the unthinkable becoming common place – nationalisation of UK banks, £200bn of money printed through the Quantative Easing programme and massive increases in public debt directly attributable to bank bail-outs.

HERITABLE

10. Heritable made its first dividend payment in July at 16.13p in the £ which was £3m. The administrator intends to make a further dividend payment in December.

11. Progress is monitored through regular conference calls of the Committee with face to face meetings quarterly. Ernst & Young, the administrator, provide a huge amount of information at these meetings which compare how the main books, mortgage lending and commercial property lending, are moving. There has been no significant adverse movement overall over the period although there are a large number of EY interventions mainly on the commercial property book. EY has not moved away from a base case position of a recovery of 80p in the £.

12. The recovery process is expected to be largely complete in 2011.

13. There is an issue relating to trust law which KCC is pursuing with the solicitors for the administrator.

GLITNIR/LANDSBANKI

14. Old Glitnir and old Landsbanki are being run by Resolution Committees. Each Resolution Committee has an Informal Creditors Committee (ICC) consisting of creditor representatives, primarily banks and bond holders. The recent announcement by Glitnir of a €750m increase in their liabilities is being followed up by creditors through the ICC meeting. This does not effect our recovery position on the basis of priority status holding.

15. The Resolution Committees are responsible for the run-off of the assets of both banks and for maximizing the returns achieved. Apart from the day to day activities the major focus this year has been negotiating financial compensation agreements between the new banks and the old banks. Solutions broadly acceptable to creditors have now been arrived at.

16. Under Icelandic law depositors, including UK local authorities, are preferred creditors. On 17 November we received notification that the Landsbanki Winding Up Board had accepted the claims from Landsbanki local authority depositers as priority claims. This is a crucial issue for the recovery. Glitnir are slightly behind in their claims filing process but we expect the same conclusion from them.

17. It is widely expected that there will be legal challenges from some creditors to this process which may delay payments being made. Once these legal challenges are resolved the claims payment process will commence.

SUMMARY

18. The projected level of recovery on Glitnir is 100% and on Landisbanki 83% - this may move higher due to the financial instrument negotiated with the new bank. With an 80% base case recovery from Heritable this would mean a loss overall of around £4m of which £2.7m relates to KCC and £1.3m to the Pension Fund.

RECOMMENDATIONS

19. Members are asked to note this report.

Nick Vickers
Head of Financial Services