

## **EXETER CITY COUNCIL**

**EXECUTIVE  
9 FEBRUARY 2010**

### **ADDITIONAL PAPER**

#### **AGENDA ITEM 3 - GENERAL FUND REVENUE ESTIMATES AND CAPITAL PROGRAMME FOR 2010/11 TO 2012/13**

##### **1. PURPOSE OF THE PAPER**

- 1.1 To update Members on the latest financial position regarding the money deposited with the Icelandic banks and the implications that this has on the Council's overall revenue budget for next year and beyond.

##### **2. BACKGROUND**

- 2.1 Members will recall that at the time of the collapse of the Icelandic banking system the Council had money on deposit with 2 of the banks directly affected. It had an investment of £3 million with Landsbanki on a short term deposit that was due to mature on 3 November 2008 and also another £2 million deposit with Glitnir Bank due to mature in early December. Both of these investments were made about a year before the collapse in November and December 2007 at a time when the credit ratings of both banks were high. The Local Government Association (LGA) together with its legal advisers has been acting on behalf of all the affected local authorities seeking recovery of the deposited sums.
- 2.2 Up until very recently the LGA had advised that the eventual payout from both banks would be in the 80% to 100% range. Although this identified a potential loss regarding the Council's Icelandic investments, the Government had allowed all local authorities to relax normal accounting rules so that any potential loss could be deferred from 2008/09 and 2009/10 until future years. In October 2009 Communities and Local Government (CLG) announced that this deferral of normal accounting requirements would end after 2010/11 and therefore this would mean that the potential loss on investments would have to be reflected in the accounts for 2010/11. At the same time CLG also advised affected local authorities that applications could be made to capitalise the potential losses during the current (2009/10) financial year. Capitalisation would allow for the loss to be spread over a number of years rather than having being charged to the revenue account all in one go. The deadline for applications to capitalise expenditure was 15 December 2009.
- 2.3 On 7 December the Council applied for capitalisation of £332,000 in respect of a potential loss on our Landsbanki investment. At the time of this application we were still expecting to recover 100% of the £2 million that was held on deposit with Glitnir bank. This was based upon the most recent advice given by the LGA and their legal advisers. On 10 December we were advised that the Winding-Up Board of Glitnir had reversed their previous decision to grant preferential creditor status to UK local authorities. This came as a great surprise and disappointment to the LGA and everyone involved, particularly as this decision was contrary to an earlier decision made by the Winding-Up Board for Landsbanki where preferential status was confirmed for UK local authorities. However, the impact of this decision upon the Council was such that it was suddenly exposed to a potentially significant loss in respect of its Glitnir deposit. As a result, the Council submitted another application for capitalisation for an additional £1.5 million bringing our total claim to £1.832 million for potential losses.

- 2.4 In order for CLG to grant approval for capitalisation they must be satisfied that each submission meets certain set criteria including the "exceptional financial difficulties test". At the time we made our submission we were and remain satisfied that we met all the criteria laid down by CLG. On 1 February 2010 the Council received a refusal letter from CLG in respect of our application to capitalise £1,832 million in respect of our potential Icelandic bank losses. It has also since become apparent that whilst some other local authorities have been successful with similar applications a significant number like ourselves have been refused. We have not yet received any specific detail as to why we were unsuccessful with our submission. In our refusal letter it simply stated that "On the basis of the information you have provided, we consider that the circumstances you describe are not sufficiently exceptional to justify the issue of a capitalisation direction in respect of impairment of Icelandic investments".
- 2.5 The impact of the refusal CLG upon the Council's revenue finances is severe. The Council is now faced with the likelihood of having to account for the potential loss of £1.832 million during the 2010/11 financial year. A revised medium term financial plan showing the full impact is attached. This shows that based upon the Council's current budget proposals, the level of the general fund balance would drop to £1 million at the end of 2010/11, and reduce even further in the subsequent two years. This is not a sustainable financial position for the Council and will therefore require robust action to ensure financial stability for the future. Over the medium term the level of the general fund balance will need to be reinstated to the minimum level of £2 million in accordance with the Council's current budget strategy.

### **3. THE NEXT STEPS**

- 3.1 The Council strongly believes that the decision taken by CLG on this matter is unsound and that it has failed to appreciate the extreme financial hardship that will be caused by refusing this capitalisation request. The Council has already made contact with both its MP Ben Bradshaw seeking his urgent help and with the Finance Director of LGA. As a result the LGA is now actively pursuing the issue with CLG on behalf of a number of similarly affected authorities.
- 3.2 If a reversal of the capitalisation decision is not made soon by CLG, then the Council will have to come up with a plan of action to restore financial stability as a matter of extreme urgency. The revised medium term plan shows that the Council's balances will drop to £1 million at the end of next year if no action is taken. Whilst in the short term the Council could function with this low level of balances, in the medium term it will be necessary to identify further savings of £1.832 million in order to restore balances to the prudent level that is required. However, having already struggled to make proposed cuts of £1 million for next year's budget it is inconceivable at the moment that we could achieve this level of savings without there being a huge impact upon services. At its meeting on 13 April the Executive will be presented with further proposals and a plan of action to address the severe financial issues that the Council is faced with.

### **4. RECOMMENDATION**

It is recommended that:

- 4.1 the report be noted;
- 4.2 the Council continues to lobby and work with other interested parties in seeking a positive capitalisation decision from CLG;

- 4.3 if a positive decision on capitalisation is not forthcoming then the Head of Treasury will report back to Executive on 13 April on possible options and actions that need to be undertaken in order to deliver a sustainable financial position for the Council in the medium term.

HEAD OF TREASURY SERVICES

CORPORATE SERVICES DIRECTORATE

**Local Government (Access to Information) Act 1985 (as amended)**

**Background papers used in compiling this report:**

None