Agenda item 12

Council's Investments in Icelandic Banks

Please note that a supplemental update report tabled at the meeting is attached at the end of this item

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Meeting	Cabinet
Date	23 October 2008
Subject	**Council Deposits in Icelandic Banks**
Report of	Leader and Cabinet Member for Resources
Summary	To report to Cabinet on the Council's exposure to Icelandic banks and resulting implications should the deposits not be repaid.

Officer Contributors	Director of Resources & Chief Finance Officer Assistant Director of Resources (Strategic Services)
Status (public or exempt)	Public
Wards affected	Not applicable
Enclosures	Appendix A – Council's Deposit Portfolio Appendix B – List of known authorities with exposure to Icelandic banks Appendix C – Joint Treasury / LGA Statement (9.10.08) Appendix D – LGA Statement (1410.08)
For decision by	Cabinet
Function of	Executive
Reason for urgency / exemption from call-in (if appropriate)	N/A

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1. RECOMMENDATIONS

1.1 That Cabinet note current position in the financial markets and the actions to be taken by the Director of Resources & Chief Finance Officer in response to the current financial climate.

1.2 That cabinet approve the amendments to the Treasury Management Strategy for 2008/09.

1.3 That authority be delegated to the Leader and Cabinet Member for Resources to agree further amendments required to the Treasury Management Strategy and for any amendments to be reported to the next meeting of Cabinet Resources Committee.

2. RELEVANT PREVIOUS DECISIONS

2.1 Council 7 January 2003 – Treasury Management Practices.

2.2 Cabinet Resources Committee 25 March 2008 – Treasury Management Business Strategy.

3. CORPORATE PRIORITIES AND POLICY CONSIDERATIONS

3.1 The Treasury Management Business Strategy ensures effective treasury management support towards the achievement of the Council's corporate priorities in achieving a better Council and a Better Barnet. It is committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

4. RISK MANAGEMENT ISSUES

4.1 The most significant risk is that the Council is unable to recover monies deposited with the Icelandic banks that have gone into receivership/administration and/or been nationalised, including any interest payments due. Actions being taken to mitigate this risk are set out in more detail in this report.

4,2 Borrowing and deposit rates are determined by the market and can be volatile at times. Officers mitigate this volatility by monitoring the interest rate market in conjunction with treasury advisors and brokers, and by actively managing the debt and deposit portfolios.

4.3 There is a risk of the Council becoming too risk averse in its response to this situation, and not achieving budgeted deposit income. In the past two years, the Treasury Management Strategy has delivered £26m interest earnings across all funds to support the council budget.

5. EQUALITIES AND DIVERSITY ISSUES

5.1 The management of the Council's cash flow ensures the availability of adequate monies to pay for the delivery of the authority's public duties.

6. USE OF RESOURCES IMPLICATIONS (Finance, Procurement, Performance & Value for Money, Staffing, IT, Property, Sustainability)

6.1 The Council has budgeted for around £10m of interest income in 2008/09.

6.2 The 2007/08 Statement of Accounts, which have been signed off by the Council's external auditors, includes £1.037m of interest which has not yet been received and therefore the accounts are potentially overstated by that amount should the interest not be paid.

6.3 During 2008/09, the deposits are due to yield a further £1.513m. This would be a combination of actual interest received as the deposits matured and further accrued interest in line with proper accounting practice.

6.4 The current average interest rate on the Council's deposits and the average daily cash balance have been higher than assumed in the budget, so it is still possible that the budgeted level of interest can still be achieved in 2008/09. The monitoring report to Cabinet Resources Committee in September highlighted an expected in year benefit of £1m, before this position with Icelandic banks emerged.

6.5 The wider financial implications for the Council are dealt with in section 9 of this report.

7. LEGAL ISSUES

7.1 The legal issues are dealt with in section 9 of this report.

8. CONSTITUTIONAL POWERS

8.1 Financial Regulations (Part 1, Section 6) within the Council Constitution state:-

(1) The Council adopts the key recommendations contained in "The Prudential Code for Capital Finance in Local Authorities – Interim Guidance & Notes Supplement" (CIPFA, February 2004), "Treasury Management in the Public services: Code of Practice" (CIPFA,2001) and any subsequent recommended good practice by CIPFA.

(2) Cabinet Resources Committee will create and maintain a Treasury Management Policy Statement, stating the policies and objectives of its treasury management activities.

(3) The Chief Financial Officer will create and maintain suitable Treasury Management Practices (TMPs), setting out the manner in which the Authority will seek to achieve those policies and objectives, and prescribing how it will manage and control these activities.

(4) Cabinet Resources Committee will receive reports on its treasury management activities, including an annual strategy and plan in advance of the year, and an annual report after its close in the form prescribed in the TMPs. These reports will incorporate the prudential borrowing limits and performance indicators.

9 BACKGROUND INFORMATION

9.1 Treasury Management Guidance

9.1.1 Treasury Management in Local Government is guided by the 2001 revision of the CIPFA Code of Practice on Treasury Management in the Public Services. The Council has adopted the code and complies with its requirements.

9.1.2 One objective of the CIPFA Code of Practice on Treasury Management and subsequent Treasury Policy Statements is to ensure that by using prudent and proper practices the financial resources of local authorities are protected and best used.

9.1.3 The Code requires the formulation and agreement of a Treasury Policy Statement and Practices, setting out responsibilities of the Council, committees and officer responsibilities/delegation and reporting arrangements. The statement and accompanying practices were approved by Council on 7 January 2003.

9.2 Treasury Management Strategy

9.2.1 Treasury management activity is governed by the annual Treasury Management Strategy, which is approved each March by the Council's Cabinet Resources Committee. The strategy is prepared in accordance with the CIPFA Code and forms an important part of the overall financial governance framework of the Council, which is taken into account each year by the external auditor as part of the Use of Resources assessment and general audit work.

9.2.2 One of the key elements of the strategy is the management of risk through an approved counterparties list the Council should place deposits with, the individual limits on the deposits placed with any counterparty, and the mix of short and long term deposit periods used. This is all designed to ensure the Council does not put all its eggs in one basket (e.g. the Western Isles Council and BCCI scenario), and to ensure that the council achieves a decent return on deposits.

9.2.3 The strategy states that the criteria used by the Council to select the counterparties with which it can place deposits are based on the long term and short term credit ratings used by the main credit rating agencies, Fitch, Moody's and Standard & Poors. The approved ratings at the time deposits were made were:-

- Short term – 'F1' (Fitch) or 'P-1' (Moody's)
- Long term – 'A' (Fitch) or 'A1' (Moody's)

A Fitch short-term rating of 'F1' is defined as being best quality grade, indicating strong capacity for timely payment of financial commitments. The strongest possible credit rating for short term is 'F1+' which is defined as being best quality grade, indicating exceptionally strong capacity of obligor to meet its financial commitments.

A long-term rating of 'A' denotes expectations of low credit risk and the capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings. The highest credit rating of 'AAA' is the

highest credit quality and denotes an exceptionally strong capacity for payment of financial commitments usually Government issued debt. 'AA' credit ratings denote expectations of low credit risk and indicate very strong capacity for payment of financial commitments. The lowest investment grade rating is 'BBB' which indicates that there are currently expectations of low credit risk. The capacity for payment of financial commitments is considered adequate but adverse changes in circumstances and economic conditions are likely to impair this capacity. Fitch issue further credit ratings below 'BB' that range to 'NR' (not reported), these grades are known as non-investment or speculative grades.

9.2.4 Section 9.10.5 recommends amendments to the current strategy to mitigate the level of risk exposure in the short term while the market stabilises.

9.3 Cash-flow Management

9.3.1 At any one point in time the Council has a significant amount of cash deposited in the money market. This cash comprises a number of things, e.g. balances and reserves, council tax income, grant income, capital receipts unapplied, business rates income, etc. It also includes amounts borrowed to fund future capital schemes as we undertake this borrowing at the most opportune time rather than the day before the capital expenditure is incurred.

9.3.2 This last point deserves a more detailed explanation. Given that some borrowing might be for 50 years or more, marginal differences in interest rates can have very significant implications for future years' budgets and council tax levels, so it is crucial to undertake borrowing at the most advantageous time to the council. This is exactly why £40m long-term borrowing for PSCIP was undertaken in 2006, to take advantage of the very low market rate loan available at that time. The PSCIP borrowing deal was deliberately structured with a primary period of six years, after which the lender could recall the advance, in the knowledge that at the end of the six years the majority of surplus lands within the programme should have been sold and the money would be available to repay the loan if it was called in. Earmarking borrowing in this way to a capital project is not the norm, but the gross value of this particular programme is substantial and the action was taken to protect the council from higher borrowing rates expected in 2008 and onwards (i.e. when the actual capital expenditure would be incurred). This prediction on interest rates has indeed occurred, and the decision was discussed with the External Auditor before being implemented.

9.3.3 As at 9 October 2008, the Council held £328.8m in deposits. Deposit of these sums by the council is not speculative activity, but clearly the manner in which surplus monies are invested has a substantial impact on council budgets. Comments in the national press suggesting councils have lazy risk management strategies, no well rounded deposit strategies, etc. are unfounded and unnecessarily damaging to the reputation of local government.

9.3.4 In 2007/08, gross interest earnings amounted to £16.2m, and a reduction in the average rate of interest achieved on deposits would have had a considerable effect on the Council's outturn and final level of balances at the year end. This represented an average 5.91% return on deposits, and in order of magnitude should be recognised as funding the entirety of the Library Service (£7.2m), Refuse Service (£5.4m), General Fund Housing Service (£1.6m), and Planning & Environment Service (£1.6m), with some funding left over. Just a 0.5% reduction in the average rate of interest earned

over the past three years would have deprived the council of £2.8m in resources, or put another way would have added 1.9% to Council Tax in 2008/09 or reduced council balances to £14.6m. Interest earned in 2007/08 represents an annual saving of £102 per Band D property or nearly £2 per week.

9.3.5 The Council's deposit portfolio as at 9 October 2008 is shown in Appendix A. This sets out the counterparty (and their country of origin), the amount deposited, the date of the deposit, the date of the repayment of the deposit and the credit rating of the counterparty at both the time of the deposit and currently.

9.3.6 So far only one major UK financial institution has declared exposure to Icelandic banks – Chelsea Building Society who had placed £50m. Given the unravelling of the US sub-prime market in the US that is widely accredited for starting this credit crunch, it is inevitable that most if not all major UK banks and building societies have exposure to Icelandic banks either directly or indirectly. They could certainly be classified as "informed investors", yet are receiving an immense level of Government financial support. This should be contrasted with the relative insignificant exposure of local authorities to this market, and who are receiving no direct support from the UK Treasury.

9.3.7 It is important to emphasise that, although they easily met the approved credit rating criteria, the major UK banks (Barclays, Lloyds TSB etc.) have not historically shown any interest in taking standard deposits from local authorities. This is primarily due to local authorities not having sufficient funds to place in a single transaction of the size these banks prefer to deal in – their position has only shifted in the last six months as the liquidity problems have affected them. Accordingly all institutions have reduced their thresholds for taking deposits and the Council began placing standard deposits with them earlier this financial year.

9.3.8 There is talk or rumour of some councils moving all their deposits into bonds and gilts[1]. Whilst this might in the first instance sound like a flight to safety, a closer scrutiny suggests there are still risks with this approach. The value of the yield on all bonds can change on a daily basis, which is directly related to price. Where there is a high demand for any particular gilt issue then the price of the gilt will rise as well as reducing the yield (i.e. they move in opposite directions). The growth in demand for these instruments over the last couple of months has resulted in a fall in yields on gilts. This all makes treasury management activity a lot more complicated, in that when planning ahead future cash flows you cannot with any certainty determine what you can sell bond and gilt holdings for – so there is a very real risk of getting back less capital than you deposited. We also do not have the expertise in house to make bond and gilt investments, something reinforced by the fact that the pension fund investment managers have dedicated teams managing this sector of the market.

9.4 Credit Crunch

9.4.1 The credit crunch is the term that has been coined for the current national crisis of a sustained period of banks having significantly reduced their lending to each other due to their uncertainty about how much money they have. The effect of this for the customers of bank has been higher rates for loans and mortgages.

[1] Gilts are Government Bonds

9.4.2 The starting point for the credit crunch was in the United States housing market as interest rates rose from 1% to 5.35% between 2004 and 2006 leading to falling house process and a rise in homeowners defaulting on their mortgages. The first major sign of a problem came in April 2007 when New Century Financial, a US Bank specialising in sub-prime mortgages (loans made to people with a poor credit history and who cannot prove their incomes) filed for bankruptcy protection. The collapse of the sub-prime mortgage market continued over the summer of 2007 with more mortgages going into default and US banks left with repossessed properties which did not cover the amount of the loans.

9.4.3 Banks across the world became increasingly reluctant to lend to each other due to concerns over not being able to recover their investments leading to the European Central Bank pumping €95 billion, followed shortly after by a further €108.7 billion, into the banking market to improve liquidity. At the same time, UK sub-prime lenders began to withdraw mortgages or put up the cost of borrowing for UK homeowners with poor credit histories.

9.4.4 In September 2007, Northern Rock suffered huge losses as a result of the sub-prime market in a similar way to banks in the US and appealed to the Bank of England for emergency help to assist its liquidity. Northern Rock relied heavily on the market rather than savers deposits to fund its mortgage lending and, as the market would not loan it funds, it turned the Bank of England as lender of last resort. This action generated widespread panic with depositors and led to customers queuing outside its branches to withdraw over £1 billion of deposits in a single day. After consultation with the Treasury and the Financial Services Authority (FSA), the Bank of England agrees to provide Northern Rock with emergency financial support. The government subsequently launches an investigation into why the FSA had not previously predicted the Northern Rock situation. Northern Rock was eventually nationalised in February 2008 which finally ceased savers withdrawing their deposits.

9.4.5 During October 2007, major international banks, such as UBS in Switzerland and Merrill Lynch in the US, begin to announce major losses as a result of exposure to bad debts, principally sub-prime loans. Many other banks followed over the next twelve months, including Barclays and Royal Bank of Scotland, and announced share issues to bolster their balance sheets against their bad debt exposure.

9.4.6 By November 2007, the interbank lending rate (LIBOR) rose to its highest level in nine years of 6.7975% and over 1% higher than the Bank of England base rate of 5.75%. This reflects the lack of liquidity in the banking sector and the level of concern of the financial stability banks had over other banks.

9.4.7 Over this period, the number of new mortgages being approved hit a three year low with the deals available at considerably higher rates than were available earlier in 2007 and indications that reductions in the Bank of England base rate were not being passed on to mortgage customers.

9.4.8 In December, the major central banks around the world, led by the US Federal Reserve, offered billions of dollars of support to banks in the form of loans. The European Central Bank offered $500 billion pounds to commercial banks to support their liquidity of the Christmas period.

9.4.9 In March 2008, Bear Stearns, the fifth largest bank in the US, was sold for a fraction of

its price after struggling with large mortgage debts and other banks not lending it sufficient money to survive. The US Federal Reserve had already made a further $200 billion available to banks and other institutions.

9.4.10 The Bank of England announced details in April 2008 of a £50 billion plan designed to help credit-squeezed banks by allowing them to swap potentially risky mortgage debts for secure government bonds.

9.4.11 In August, US mortgage lender IndyMac collapsed, the US government effectively nationalised two banks, Fannie Mae and Freddie Mac, and this was followed in September by America's fourth largest investment bank, Lehman Brothers, filing for bankruptcy protection once it became apparent that there was not an interested buyer. By the end of that week, Merrill Lynch had agreed to be taken over by the Bank of America.

9.4.12 Also in September, the US Federal Reserve announced an $85 billion rescue package for the largest US insurance firm, AIG, to save it from bankruptcy in return for a large public stake in the firm. The US Congress and Senate, eventually, agreed a $700 billion rescue package to safeguard the US banking system.

9.4.13 In the UK, the largest mortgage lender, Halifax Bank of Scotland (HBOS) is taken over by Lloyds TSB having seen half year profits sink by 72% and bad debts rise by 36%.

9.4.14 This month has seen the International Monetary Fund, central banks and governments around the world all moving to support the banking system.

9.4.15 Following on from Northern Rock in February, Bradford & Bingley is nationalised with the government taking control of the bank's £50 billion mortgages and loans while its savings operations and branches are sold to Santander. In Iceland, the government moved to take control of Glitner, the country's third largest bank, after the company faced short term funding problems. Wachovia, the fourth largest bank in the US, is bought by a rival in a package backed by the US authorities. Dexia is rescued after a joint injection of £5 billion by the Belgian, French and Luxembourg governments. Germany announced a deal, privately brokered with banks, to rescue Hypo Real Estate worth £38.7 billion.

9.4.16 Icelandic bank Landsbankii was declared insolvent and the UK government has moved to freeze all the UK held assets of the bank.

9.5 Iceland and the Icelandic Banks

9.5.1 What is emerging now is that the backdrop to the Icelandic bank situation is the Icelandic economy having suffered from sustained high levels of inflation which has pushed interest rates in excess of fifteen per cent. In such a small economy, this has attracted currency speculators, leading to a large inflow of foreign currency, a sharp exchange rate increase, giving the Icelanders an illusion of wealth. This ultimately led to an inevitable correction in the exchange rate and a rapid depreciation of the Krone, but the Icelandic central bank did not prepare for this occurrence by establishing adequate reserves.

9.5.2 The second factor was the relative gearing of the banking industry in Iceland. Prior

to recent events, the Icelandic banks had foreign assets worth approximately ten times the country's gross domestic product with an equivalent level of debt. In relative terms, this was a better position than many other European banks and a situation that was generally improving with the banks seeking to improve their balance sheets by seeking deposits. So the banks were not affected by the sub-prime issues that affected Northern Rock and many of the other banks to have subsequently come under pressure.

9.5.3 The problem faced by Icelandic banks comes during periods of financial uncertainty when the market looks for an implicit or explicit guarantee from the state to support the liquidity of banks. Due to the relative size of the banks to the level of net assets held by the state, the Icelandic government was not in a position to do this unlike other European countries.

9.6 Impact on the Council and Public Sector

9.6.1 Though the total figure is still becoming clear, initial figures indicate that over one hundred local authorities held deposits totalling over £800m with Icelandic banks.

9.6.2 The Council has £27.4m deposited in two Icelandic banks, Glitner Bank and Landsbankii, placed between November 2006 and September 2007. These deposits are due to be repaid between November 2008 and September 2010. At the time of writing this report the most comprehensive list of local authorities affected (published by the BBC) is attached at Appendix A, although it is known that this list is not complete.

9.6.3 At the time the deposits were made, both banks had long term 'A' ratings with widely used industry credit rating agencies. The long term rating of Glitner Bank only reduced below 'A' (the Council's limit for dealing with a counterparty) in May 2008 and the Council placed no further deposits with this bank from this date. The long term rating of Landisbanki Bank only reduced below 'A' on 30 September 2008.

9.6.4 Even after the banks had been downgraded, the Council was unable to recover the funds as it had entered long term contracts with the banks and would have been subject to significant penalties for making the withdrawals. Glitner bank's London office has said they would not have repaid our deposits 6 months ago, however they would have considered repayment 18 months ago but the depositor would have had to pay the replacement costs of Glitner arranging alternative funding. Replacement costs would include brokerage and any underlying derivatives that the bank may have entered into with other banks. Landisbanki gave a similar response when their office in Iceland was contacted.

9.6.5 The joint statement from the Government and the Local Government Association (LGA) on 9 October 2008 (see Appendix C) stated that that there was no evidence of recklessness by local authorities. They also agreed that local authorities were correct to operate within a financial framework that struck an appropriate balance between security of deposits and returns, and that it appeared this framework had been adhered to.

9.6.6 As noted above, the Council merges all available funds of the General Fund, HRA, Pension Fund, capital programme etc. together to maximise returns on its deposits. Therefore, any attempt to separate out the potential impact of not recovering the funds

would be notional at this stage.

9.6.7 In addition to the potential (whole or partial) loss of the deposit itself, there is also the potential loss of the interest as well. As the deposits were placed in either 2006/07 or 2007/08, the Council has already accrued in the accounts up to 31 March 2008 for £1.037m of deposit interest, which may not be received. The total amount of interest due up to the date of each deposit maturing is £4.463m.

9.6.8 It is important to emphasise that this situation does not impact at this time on the Council's ability to pay its staff and suppliers in the short term. The first of the deposits was due to be repaid next month and the Council's cash flow will need to be managed to ensure that the authority can continue to meet all liabilities.

9.7 Response of UK Government

9.7.1 As the Icelandic position began to develop, the Prime Minister Gordon Brown hit out at the Icelandic Government for its "totally unacceptable" response to the folding of institutions like Landsbanki and Glitnir. Threatening legal action, he insisted it was the responsibility of Iceland's authorities to reimburse UK investors who stood to lose their deposits. He further said "This is a problem that has been caused by Iceland. It is totally unacceptable behaviour. … There is a responsibility on the Icelandic authorities to respond. They are the regulators, they are the supervisors, they are the people responsible for what the Icelandic banks based in Iceland are doing, and we expect them to honour their obligations."

9.7.2 In respect to UK local authorities, however, the UK Treasury response has so far been muted, with no sign of any offer of direct financial support to local authorities – compared to the (£300bn, or whatever the true figure really is) being offered to retail depositors and UK banks and other financial institutions. The Government has indicated that assistance will be given to councils but no clear indication has been made at present. If local authorities do eventually have to make write-offs, it's possible that this will be supported by allowing councils to capitalise this cost in order to spread the cost over a period of years.

9.7.3 Government's focus with local authorities has been on assisting where short term cash flow issues, i.e. unable to pay staff and suppliers, or medium term risks to balances. There has been no blanket statement, of support or otherwise, with the Government commenting that it will look at providing assistance on a case by case basis with possible solutions being capitalisation directions or providing financial expertise to authorities through a rapid response unit. It is unclear at the time of writing as to how these will be used to assist local authorities.

9.7.4 Government has been clear in its statements that local authorities are 'wholesale creditors' and therefore are not in a position to get the support offered to the general public who have saved with the institutions. Though £50 billion has been made available in support of the major banking institutions, and a larger amount has been put in to support the banking system generally in this country, no statements of support have, at the time of writing, been offered by the Government for local authorities. Conversely, local authorities have been identified as 'informed investors' who should have been aware of the risks and therefore have to bear the loss.

9.7.5 The Government has moved to freeze the UK assets of the Icelandic banks to ensure

the return of deposits held by individuals.

9.7.6 A Treasury delegation, including officials from the Bank of England and the Financial Services Authority, has been sent to Iceland to seek assurances that UK savers will not lose their deposits and to establish a claims procedure for British savers to get their money back as soon as possible. The delegation is also pressing for the quick return of the £1 billion of deposits that relate to local authorities and other public sector bodies.

9.7.7 The 15 Eurozone Leaders have been meeting in Paris to work further on a skeleton plan developed by the G7 leaders at a summit in Washington. The plan is to develop a common approach to the financial crisis though it will not result in a joint financial rescue fund for Europe akin to the $700 billion rescue by the US government.

9.7.8 On 14 October 2008, the LGA made a further statement – see Appendix

9.8 Response of other Governments outside of the UK and Iceland

9.8.1 The council has deposits placed in other overseas banks. The position in each of those countries is summarised below:-

- Ireland

  The Irish Government on 30 September 2008 provided a guarantee for all deposits at Allied Irish Banks, Anglo Irish Bank Corporation, Bank of Ireland, EBS Building Society, Irish Nationwide Building Society and Irish Life & Permanent. This guarantee covers all new and existing facilities until 28 September 2010.

- Belgium

  Irish Intercontinental is a subsidiary of KBC bank, which is headquartered in Brussels, Belgium and has a Fitch long term rating of AA- and a short term rating of F1+.

- United Arab Emirates (UAE)

  The UAE Government on 12 October 2008 stated it would guarantee all bank deposits and savings in the UAE's national banks and interbank lending, and inject as much liquidity into the system as necessary.

- Saudia Arabia

  The Government has also stated it would make £23bn available to its banks if needed.

- Germany

  Hypo Real Estate Group, of which Depfa bank is part of, has agreed a short-term multi-billion euro credit facility with a consortium of German banks, which will be succeeded by a EUR35bn secured funding facility provided by the

European Central Bank that is backed by a guarantee from the Federal Republic of Germany.

We are working to provide a more comprehensive briefing on the position with other overseas deposits for the Cabinet meeting.

9.9 Planned Actions

9.9.1 The Council is lobbying and will continue to lobby the Government for support, both directly and through organisations such as the LGA and London Councils.

9.9.2 Officers in Resources and Corporate Governance will work through the legal implications of the banks going into receivership and the mechanisms for ensuring the return of the Council's deposits.

9.9.3 As noted above, it is necessary to change the Council's Treasury Management Strategy, with the changes detailed in section 9.10, to ensure officers can continue to manage the Council's cash flow with an appropriate level of risk in these exceptional global circumstances. The strategy will remain under constant review, and agreement is requested to delegate authority to the Leader and Cabinet Member for Resources to agree any further changes required with any such changes reported to the Cabinet Resources Committee in December.

9.9.4 In the event that the Council does not recover the £27.4m deposit and/or the interest due on those deposits, it will have to consider appropriate actions to mitigate those losses, including:-

- writing off the interest already accrued by drawing down on balances and reserves;
- writing off the proportion of the principal to the General Fund, Housing Revenue Account and Pension Fund;
- reviewing the capital programme to identify the scope to reduce or re-phase existing capital schemes;
- reviewing the timing of future large payments, such as those linked to major capital projects, to enable the re-profiling of the Council's cash flow;
- seeking alternative sources of external funding for projects to reduce the requirement for prudential borrowing;
- reviewing reserves and balances to draw down to reduce impact on service delivery;
- reviewing all service budgets to identify potential savings and service reductions that can be taken straight away to mitigate the impact on balances.

9.10 Changes to the Treasury Management Strategy 2008-09

9.10.1 It is necessary to make amendments to the current treasury management strategy to

mitigate the level of risk exposure in the short term while the market stabilises.

9.10.2 One of the key elements of the strategy is the management of risk through the approved counterparties the Council can place deposits with, the individual limits on the amount that can be placed with any individual or group of counterparties and that a range of deposit periods is employed. The limit in the strategy approved by Cabinet Resources Committee was a maximum £15m with any single counterparty or group.

9.10.3 The strategy also states that the basis on which the Council selects counterparties is the long and short term credit ratings used by the main credit rating agencies – Fitch, Moody's and Standard & Poors, or the relevant ranking for building societies where no conventional rating exists.

9.10.4 In light of recent events it is proposed to raise the minimum credit rating of counterparties by two categories from the Fitch long-term rating of A to AA- and short-term rating of F1 to F1+ or the Standard & Poors and Moodys equivalent. This will inevitably reduce the number of available institutions to place deposits with, so to enable the Treasury Management team to maintain some flexibility it is proposed to increase the maximum counterparty limit to £25m. Whilst this increases the exposure of the Council to a single bank doing so alongside increasing the credit rating of those banks will mitigate that risk.

9.10.5 The table below shows the current and proposed new limits for placing deposits with counterparties.

	Current	Proposed
Credit rating	Fitch long-term rating A and short-term rating F1 or Moodys and Standard & Poors equivalent rating. Top twelve building societies as per the Building Societies Association asset list.	Fitch long-term rating AA- and short-term rating F1+ or Moodys and Standard & Poors equivalent rating.
Counterparty limit	£15m	£25m

9.10.6 The only exception to the above credit ratings will be where there is an explicit state guarantee of depositors funds, for example as currently exists with the Irish government. Even allowing for this, such institutions would only be used as a backstop where no other options exist with banks that meet the revised criteria above and would be placed for a maximum period less than that guaranteed by the state.

9.10.7 Because events continue to develop on a daily basis, further material, public and/or exempt is likely to be circulated before the meeting in order to keep members up-to-date.

10. LIST OF BACKGROUND PAPERS

10.1 None

Legal: JEL
CFO: CM/JB

Appendix A

Council's deposit portfolio as at 9th October 2008

Counterparty name	Amount £	Start date	Maturity	Fitch rating when deal done		Fitch rating Curent rating	
				Long-term	Short-term	Long-term	Short-term
Abbey	1,600,000	20-Aug-08	CALL	AA-	F1+	AA-	F1+
Alliance & Leicester	4,200,000	26-Aug-08	26-Nov-08	A+	F1	A+	F1
	3,000,000	21-Jan-08	21-Oct-08	AA-	F1+	A+	F1
	3,000,000	21-Jan-08	21-Jan-09	AA-	F1+	A+	F1
	1,700,000	10-Sep-08	10-Dec-08	A+	F1	A+	F1
Allied Irish Bank	9,500,000	24-Aug-07	CALL	AA-	F1+	AA-	F1+
Anglo Irish Bank	2,750,000	25-Jun-08	18-Mar-09	A	F1+	A+	F1
	250,000	14-Feb-06	CALL	A	F1+	A+	F1+
Arab National Bank	6,500,000	08-Sep-08	31-Dec-08	A	F1	A	F1
	5,000,000	15-Apr-08	15-Oct-08	A	F1	A	F1
	2,500,000	11-Aug-08	27-Oct-08	A	F1	A	F1
	1,000,000	31-Jul-08	31-Oct-08	A	F1	A	F1
Bank Of Ireland	9,000,000	03-Sep-08	CALL	AA-	F1+	AA-	F1+
	5,000,000	10-Sep-08	31-Oct-08	AA-	F1+	AA-	F1+
	1,000,000	09-Jul-08	31-Oct-08	AA-	F1+	AA-	F1+
Bank Of Scotland - Ireland	11,000,000	14-Jul-08	14-Jul-09	AA+	F1+	AA	F1+
	4,000,000	02-Jul-08	31-Oct-08	AA+	F1+	AA	F1+
Barclays	7,000,000	07-Mar-08	07-Mar-13	AA+	F1+	AA	F1+
Bradford & Bingley Plc	2,200,000	30-May-08	28-Nov-08	A	F1	BBB-	F3
Britannia BS	5,000,000	11-Sep-08	02-Jan-09	A+	F1	A	F1
	2,800,000	08-Jul-08	31-Oct-08	A	F1	A	F1
	2,000,000	20-Aug-08	01-Dec-08	A	F1	A	F1
	1,500,000	06-Jun-08	08-Jun-09	A	F1	A	F1
Cater Allen Bank	10,000,000	04-Aug-08	04-Aug-09	AA-	F1+	AA-	F1+
Chelsea Building Soc.	10,000,000	08-Sep-08	08-Dec-08	A	F1	A	F1
	2,000,000	31-Jul-08	31-Oct-08	A	F1	A	F1
	1,500,000	08-Sep-08	08-Dec-08	A	F1	A	F1
	1,400,000	11-Apr-08	10-Oct-08	A	F1	A	F1
Cheshire BS	4,000,000	22-Sep-08	23-Dec-08	A3	P-2	A3	P-2
	3,000,000	05-Sep-08	19-Dec-08	A3	P-2	A3	P-2
	2,300,000	07-Aug-08	07-Nov-08	A3	P-2	A3	P-2
Coventry Building Soc.	8,100,000	15-Sep-08	30-Jan-09	A	F1	A	F1
	3,000,000	17-Sep-08	30-Jan-09	A	F1	A	F1

Counterparty name	Amount £	Start date	Maturity	Fitch rating when deal done		Fitch rating Curent rating	
				Long-term	Short-term	Long-term	Short-term
	2,000,000	21-May-08	21-May-09	A	F1	A	F1
	1,500,000	03-Jul-08	31-Oct-08	A	F1	A	F1
Depfa Bank	3,000,000	07-Jul-08	17-Oct-08	A	F1	A-	F1
	3,000,000	30-May-08	28-Nov-08	A	F1	A-	F1
	2,200,000	20-Aug-08	01-Dec-08	AA-	F1+	A-	F1
	2,000,000	07-Feb-08	07-Nov-08	AA-	F1+	A-	F1
Derbyshire BS	5,000,000	08-Sep-08	08-Dec-08	A2	P-2	A2	P-2
	2,600,000	05-Sep-08	01-Dec-08	A2	P-2	A2	P-2
	2,000,000	07-Aug-08	07-Nov-08	A2	P-2	A2	P-2
EBS	5,000,000	05-Feb-08	05-Nov-08	A	F1	A	F1+
	4,000,000	05-Sep-08	19-Dec-08	A	F1	A	F1+
Glitner Bank (Iceland)	7,000,000	07-Nov-06	07-Nov-08	A	F1	BBB-	F3
	3,000,000	24-Jan-07	24-Mar-09	A	F1	BBB-	F3
	2,400,000	07-Feb-07	09-Feb-09	A	F1	BBB-	F3
HBOS	5,000,000	29-May-07	29-May-12	AA+	F1+	AA	F1+
	5,000,000	21-Apr-08	21-Apr-09	AA	F1+	AA	F1+
Irish Intercontinental	7,000,000	18-Sep-08	31-Oct-08	A+	F1	A+	F1
	5,400,000	15-Aug-08	15-Oct-08	A+	F1	A+	F1
Irish Nationwide	6,200,000	01-Oct-08	01-Apr-09	A	F1	A	F1+
	5,000,000	06-Oct-08	27-Feb-09	A	F1	A	F1+
	2,000,000	06-Feb-08	06-Nov-08	A	F1	A	F1+
Landisbanki Islands H.F.	15,000,000	28-Sep-07	28-Sep-10	A	F1	BBB	F3
Leeds BS	2,800,000	20-Aug-08	26-Nov-08	A	F1	A	F1
	2,500,000	21-Aug-08	26-Nov-08	A	F1	A	F1
	2,500,000	29-Sep-08	30-Jan-09	A	F1	A	F1
National Bank Of Abu Dhabi	5,000,000	17-Mar-08	17-Mar-09	AA-	F1+	AA-	F1+
	3,500,000	03-Jul-08	31-Oct-08	AA-	F1+	AA-	F1+
	1,300,000	09-Sep-08	07-Jan-09	AA-	F1+	AA-	F1+
Nationwide BS	1,500,000	15-Jul-08	15-Jan-09	AA-	F1+	AA-	F1+
Newcastle Building Soc.	5,000,000	14-Apr-08	14-Oct-08	A	F1	A	F1
	3,000,000	02-Oct-08	27-Feb-09	A	F1	A	F1
	2,000,000	02-Oct-08	06-Feb-09	A	F1	A	F1
Principality Building Soc.	4,000,000	02-Oct-08	30-Jan-09	A	F1	A	F1
	2,500,000	16-Apr-08	16-Jan-09	A	F1	A	F1
	2,500,000	29-Sep-08	30-Jan-09	A	F1	A	F1
	1,000,000	20-Aug-08	01-Dec-08	A	F1	A	F1
Riyad Bank	12,000,000	14-Jul-08	28-Nov-08	A	F1	A+	F1
	3,000,000	15-Jul-08	15-Jan-09	A	F1	A+	F1
Royal Bank Of Scotland	5,000,000	25-May-07	25-May-11	AA	F1+	AA	F1+
	5,000,000	17-Jun-08	17-Jun-13	AA	F1+	AA	F1+

Counterparty name	Amount £	Start date	Maturity	Fitch rating when deal done		Fitch rating Curent rating	
				Long-term	Short-term	Long-term	Short-term
Skipton BS	5,000,000	08-Aug-08	24-Nov-08	A	F1	A	F1
	3,000,000	29-May-08	29-May-09	A	F1	A	F1
West Bromwich BS	3,600,000	19-Jun-08	18-Jun-09	A	F1	A	F1
	3,000,000	10-Jul-08	31-Oct-08	A	F1	A	F1
	3,000,000	03-Jul-08	05-Jan-09	A	F1	A	F1
Yorkshire BS	10,000,000	15-Jul-08	23-Dec-08	A+	F1	A	F1
	3,000,000	09-Jul-08	31-Oct-08	A+	F1	A	F1
	2,000,000	17-Sep-08	30-Jan-09	A+	F1	A	F1
	328,800,000						

Summary of banks

Counterparty name	Amount GBP	Country of origin
BANK OF SCOTLAND - IRELAND	15,000,000.00	UK
HBOS	5,000,000.00	UK
BARCLAYS	7,000,000.00	UK
HSBC	5,000,000.00	UK
ROYAL BANK OF SCOTLAND	10,000,000.00	UK
Abbey + Cater Allen	11,600,000.00	UK
ALLIANCE & LEICESTER	11,900,000.00	UK
BRADFORD AND BINGLEY PLC	2,200,000.00	UK
UK Banks	**67,700,000.00**	
Nationwide BS	1,500,000.00	UK
Britannia BS	11,300,000.00	UK
Chelsea Building Soc.	14,900,000.00	UK
Coventry Building Soc.	14,600,000.00	UK
Leeds BS	7,800,000.00	UK
Newcastle Building Soc.	10,000,000.00	UK
Principality Building Soc.	10,000,000.00	UK
Skipton BS	8,000,000.00	UK
West Bromwich BS	9,600,000.00	UK
Yorkshire BS	15,000,000.00	UK
Cheshire BS	9,300,000.00	UK
Derbyshire BS	9,600,000.00	UK
UK Building Societies	**121,600,000.00**	
DEPFA BANK	10,200,000.00	German
GLITNER BANK (ICELAND)	12,400,000.00	Icelandic
LANDISBANKI ISLANDS H.F.	15,000,000.00	Icelandic
ALLIED IRISH BANK	9,500,000.00	Irish
BANK OF IRELAND	15,000,000.00	Irish
ANGLO IRISH BANK	3,000,000.00	Irish
IRISH INTERCONTINENTAL	12,400,000.00	Irish
EBS	9,000,000.00	Irish
IRISH NATIONWIDE	13,200,000.00	Irish
RIYAD BANK	15,000,000.00	Saudi Arabia

ARAB NATIONAL BANK	15,000,000.00	Saudi Arabia
NATIONAL BANK OF ABU DHABI	9,800,000.00	United Arab Emirates
Non-UK	**139,500,000.00**	
Total	**328,800,000.00**	

BBC : list of known authorities with exposure to Icelandic banks

- Kent County Council - £50 million
- Nottingham City Council - £42 million
- Haringey - £37 million
- Norfolk County Council - £32.5 million
- Dorset County Council - £28.1 million
- Hertfordshire - £28 million
- Barnet Council- £27 million
- Somerset County Council - £25 million
- Northumberland County Council - £23 million
- Surrey County Council - £20 million
- Hillingdon Council - £20 million
- Neath Port Talbot Council - £20 million
- Westminster Council - £17 million
- Brent - £15 million
- Caerphilly County Council - £15 million.
- North Ayrshire - £15 million
- Plymouth City Council £13 million
- Havering Council - £12.5 million
- West Sussex - £12.9 million
- Breckland Council - £12 million
- Gloucestershire County Council - £12 million
- Cheltenham Borough Council - £11 million
- Lancashire County Council - £10 million
- Scottish Borders Council - £10m
- Cambridge City Council - £9 million
- Wakefield - £9 million
- West Oxfordshire District Council - £9 million
- Wyre Forest District Council - £9 million
- Cheshire County Council - £8.5 million
- Bassetlaw District Council - £8 million
- Bristol City Council - £8 million
- Daventry District Council - £8 million
- Wiltshire County Council - £8 million
- South Lanarkshire Council - £7.5 million
- Derwentside District Council - £7 million
- North East Lincolnshire Council - £7 million
- West Lindsey District Council - £7 million
- Cherwell District Council - £6.5 million
- Redcar and Cleveland Council - £6 million
- Lancaster City Council - £6 million
- Canterbury City Council - £6 million
- Ceredigion - £5.5 million
- North Lincolnshire Council - £ 5.5 million
- Sutton Council - £5.5 million
- Bracknell Forest - £5 million
- Bromley Borough Council - £5 million
- Buckinghamshire County Council - £5 million
- Stoke-on-Trent Council - £5 million

- Braintree District - £5 million
- Cornwall County Council - £5 million
- Exeter City Council - £5 million
- Ipswich Borough Council - £5 million
- Oxfordshire County Council - £5 million
- South Ayrshire - £5 million
- South Ribble - £5 million
- Wokingham Borough Council - £5 million
- Gateshead Council - £4.5 million
- Oxford City Council - £4.5 million
- Colchester Borough Council - £4 million
- East Lindsey District Council - £4 million
- East Staffordshire Borough Council - £4 million
- North Wiltshire District Council - £4 million
- Powys Council £4 million
- Restormel Borough Council - £4 million
- Rotherham Council - £3.8 million
- Flintshire Council - £3.7 million
- Aylesbury District Council - £3 million
- East Ayrshire - £3 million
- North Somerset - £3 million
- Doncaster Council - £3 million
- Nuneaton and Bedworth - £3 million
- Peterborough City Council - £3 million
- Rhondda Cynon Taff Council - £3 million
- Solihull Council - £3 million
- Stroud - £3 million
- Slough Council - £2.5 million
- South Oxfordshire District Council - £2.5 million
- Wycombe District Council - £2.5 million
- Cotswold District Council - £2 million
- Gloucester City Council - £2 million
- Great Yarmouth - £2 million
- Moray Council - £2 million
- Newark and Sherwood District Council - £2 million
- South Hams District Council - £1.25 million
- Monmouthshire Council - £1.2 million
- Mid-Devon - £1.1 million
- Charnwood Borough Council - £1 million
- Dover District Council - £1 million
- Bridgend Council - £1 million
- Bridgnorth - £1 million
- Hertsmere Borough Council - £1 million
- Kirklees Council - £1 million
- Perth and Kinross Council - £1 million
- Tewkesbury Borough Council - £1 million
- Vale of White Horse District Council - £1 million
- Winchester - £1 million
- Sevenoaks District Council - £1 million
- Tonbridge and Malling Borough Council - £1 million
- Lewes District Council - £1 million
- Burnley Council - TBC

- Chorley Council - TBC
- Wychavon District Council - TBC

Other affected public bodies

- Transport For London - £40 million
- Metropolitan Police - £30 million
- Dorset Police Authority - £7 million
- Sussex Police Authority - £6.8 million
- West Yorkshire Police Authority - £6 million
- Northumbria Police Authority - £3.5 million
- Hertfordshire Police Authority - £3 million
- Gwent Police Authority - £1 million

Joint statement from Government and LGA on Landsbanki deposits (9.10.08)

We had a very productive meeting and we agreed to stay in close touch, meeting again next week. Government and the LGA agreed that there is no evidence of recklessness by local authorities. They also agreed the financial framework for local authorities, which requires them to strike an appropriate balance between security of investments and returns, appears to have been adhered to.

Many authorities have already publicly stated that any risk is not a threat to frontline services but a small number of authorities may have specific problems.

We agreed once the LGA completed its analysis of the effects of the situation on individual local authorities, we will look at issues arising on a case by case basis. For those local authorities who are facing severe short term difficulties Government and the LGA will agree an appropriate set of ways to assist. We will judge what is appropriate on a case by case basis but in previous situations support has included helping local authorities restructure their financial priorities, providing additional expertise and capitalisation of expenditure.

The Government and international partners have already acted to support stability of the banking system. Action has also been taken in relation to the position of Icelandic banks – including freezing assets of Landsbanki. Local authorities, along with all other investors, will benefit. The LGA will be seeking to open discussions with administrators of the UK subsidiaries. The LGA and Government encourages all councils to continue operating investments in accordance with the guidance.

LGA and Government will continue to monitor the situation closely.

Appendix D

LGA Statement (14 October 2008)

The Local Government Association has today called for a Government inquiry, led by the Financial Services Authority, into how credit ratings agencies continued to give Icelandic banks high credit ratings right up until a matter of days before they went into administration or receivership.

The call came as the LGA:-

- Reveals the outcome of encouraging discussions with the administrators Ernst & Young. The administrators consider that that the value of the book value of the assets of Heritable Bank Plc and Kaupthing Singer & Friedlander Limited (both in administration) appeared to be of the same order of magnitude as the liabilities.

- Publishes an update on how many councils have been affected, which shows that 116 councils are currently known to have had deposits in Icelandic banks, with deposits totalling £858.3m.

- Calls on councils that invested after the credit ratings were downgraded to an unacceptable level on 30 September 2008 to carry out their own inquiries to discover what happened.

Analysis by the LGA of the ratings issued by the main credit ratings agencies shows that Icelandic banks and their UK subsidiaries continued to receive relatively high ratings up until the afternoon of 30 September.

Analysis shows that:-

28 February
Fitch's long-term ratings for Glitnir Bank h.f (Glitnir), Kaupthing Bank h.f (Kaupthing) and Landsbanki Islands (Landsbanki) were all A. Their corresponding short-term ratings were all F1. Moody's reduced its long-term rating for Landsbanki from Aa3 to A2, and held their short-term rating at F1. Its long-term and short-term ratings for Glitnir were Aa3 and F1 respectively.

April
Fitch announces that Icelandic banks were being put on negative rating watch, warning that short and long term ratings on Icelandic banks could be reduced.

9 May
Fitch reduced the ratings for Glitnir and Kaupthing to A minus (long-term) and F2 (short-term). Landsbanki's ratings remained the same but the outlook rating was changed to Outlook Negative.

30 September
Fitch reduced Landsbanki's long-term ratings from A to BBB and its short-term ratings from F1 to F3. The long-term and short-term ratings for Glitnir were reduced to BBB minus and F3 respectively. The long-term and short-term ratings for Kaupthing were reduced to BBB and F3 respectively. Moody's announced it was reviewing Landsbanki's ratings.

8 October
There was a general downgrade of the Icelandic banks' ratings.

Cllr Margaret Eaton, Chairman of the LGA, said:

"This isn't the time for a blame game. This is an unprecedented situation, the extent of which could not have been forseen. However, at the appropriate moment, there needs to be a full and independent inquiry to find out just how these banks continued to get relatively strong credit ratings until a few days before they went under.

"No council should rely solely on credit agencies and must use their financial nous. But there must be confidence in credit ratings as councils continue to invest billions of pounds in a whole range of financial institutions. Our analysis dispels the myth that many councils were investing recklessly after credit warnings were issued.

"The good news for council taxpayers is that discussions with the administrators have been hugely encouraging. The administrators considered that the book value of the assets of each business appeared to be of the same order of magnitude as the liabilities, although it is too early to give exact figures.

"The evidence shows that, overwhelmingly, town halls have acted prudently and within strict guidelines to get the best rates of interest on savings whilst investing in institutions deemed to be strong. If it is discovered that individual councils invested significant sums following the credit rating downgrading, the LGA expects them to set up their own inquiries to find out what happened.

"Prudent financial management means that councils put their money into a diverse range of banks to make sure that any risk is spread to minimise the impact of problems in the financial markets. We are not aware of councils that are in serious imminent liquidity problems and in the long term we are confident that vital frontline services will remain unaffected.

ENDS

AGENDA ITEM: 12 (update) Page nos. 1 – 16

Meeting	Cabinet
Date	23 October 2008
Subject	**Council Deposits in Icelandic Banks – supplementary report**
Report of	Leader and Cabinet Member for Resources
Summary	The report circulated with the agenda referred to further information that may become available.

Officer Contributors	Director of Resources & Chief Finance Officer Assistant Director of Resources (Strategic Services)
Status (public or exempt)	Public
Wards affected	Not applicable
Enclosures	Appendix A – Updated counterparty list (large sheet) Appendix B – Irish Government guarantee update
For decision by	Cabinet
Function of	Executive
Reason for urgency / exemption from call-in (if appropriate)	N/A

Contact for further information: Jonathan Bunt on 0208 359 7249 or Patrick Towey on 0208 359 7119

1. RECOMMENDATIONS

1.1 That Cabinet note current position in the financial markets and the actions to be taken by the Director of Resources & Chief Finance Officer in response to the current financial climate.

1.2 That Cabinet approve the amendments to the Treasury Management Strategy for 2008/09, after having taken into account the option on continuing to deposit or not with building societies other than Nationwide and in Irish banks.

1.3 That authority be delegated to the Leader and Cabinet Member for Resources to agree further amendments required to the Treasury Management Strategy and for any amendments to be reported to the next meeting of Cabinet Resources Committee.

2. RELEVANT PREVIOUS DECISIONS

2.1 Council 7 January 2003 – Treasury Management Practices.

2.2 Cabinet Resources Committee 25 March 2008 – Treasury Management Business Strategy.

3. CORPORATE PRIORITIES AND POLICY CONSIDERATIONS

3.1 The Treasury Management Business Strategy ensures effective treasury management support towards the achievement of the Council's corporate priorities in achieving a better Council and a Better Barnet. It is committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

4. RISK MANAGEMENT ISSUES

4.1 The most significant risk is that the Council is unable to recover monies deposited with the Icelandic banks that have gone into receivership/administration and/or been nationalised, including any interest payments due. Actions being taken to mitigate this risk are set out in more detail in this report.

4,2 Borrowing and deposit rates are determined by the market and can be volatile at times. Officers mitigate this volatility by monitoring the interest rate market in conjunction with treasury advisors and brokers, and by actively managing the debt and deposit portfolios.

4.3 There is a risk of the Council becoming too risk averse in its response to this situation, and not achieving budgeted deposit income. In the past two years, the Treasury Management Strategy has delivered £26m interest earnings across all funds to support the council budget.

5. EQUALITIES AND DIVERSITY ISSUES

5.1 The management of the Council's cash flow ensures the availability of adequate monies to pay for the delivery of the authority's public duties.

6. USE OF RESOURCES IMPLICATIONS (Finance, Procurement, Performance & Value for Money, Staffing, IT, Property, Sustainability)

6.1 At the time of writing this report it is important to stress that the council has not as yet incurred any loss.

6.2 The Council has budgeted for around £10m of interest income in 2008/09.

6.3 The 2007/08 Statement of Accounts, which have been signed off by the Council's external auditors, includes £1.037m of interest which has not yet been received and therefore the accounts are potentially overstated by that amount should the interest not be paid.

6.4 During 2008/09, the deposits are due to yield a further £1.513m. This would be a combination of actual interest received as the deposits matured and further accrued interest in line with proper accounting practice.

6.5 The current average interest rate on the Council's deposits and the average daily cash balance have been higher than assumed in the budget, so it is still possible that the budgeted level of interest can still be achieved in 2008/09. The monitoring report to Cabinet Resources Committee in September highlighted an expected in year benefit of £1m, before this position with Icelandic banks emerged.

6.6 The wider financial implications for the Council are dealt with in section 9 of this report.

7. LEGAL ISSUES

7.1 None.

8. CONSTITUTIONAL POWERS

8.1 Financial Regulations (Part 1, Section 6) within the Council Constitution state:-

(1) The Council adopts the key recommendations contained in "The Prudential Code for Capital Finance in Local Authorities – Interim Guidance & Notes Supplement" (CIPFA, February 2004), "Treasury Management in the Public services: Code of Practice" (CIPFA,2001) and any subsequent recommended good practice by CIPFA.

(2) Cabinet Resources Committee will create and maintain a Treasury Management Policy Statement, stating the policies and objectives of its treasury management activities.

(3) The Chief Financial Officer will create and maintain suitable Treasury Management Practices (TMPs), setting out the manner in which the Authority will seek to achieve those policies and objectives, and prescribing how it will manage and control these activities.

(4) Cabinet Resources Committee will receive reports on its treasury management activities, including an annual strategy and plan in advance of

the year, and an annual report after its close in the form prescribed in the TMPs. These reports will incorporate the prudential borrowing limits and performance indicators.

9 BACKGROUND INFORMATION

9.1 Further explanation of bank credit ratings

9.1.1 Fitch, Standard & Poors, and Moodys are credit rating agencies that assign credit ratings for issuers of certain types of debt obligations as well as the debt instruments themselves.

9.1.2 A credit rating for an issuer takes into consideration the issuer's credit worthiness (its ability to pay back a loan), which in turn affects the interest rate applied to the particular security being issued.

9.1.3 Credit ratings are used by investors, issuers, investments banks, broker-dealers, other depositors and governments.

<u>Types of credit rating</u>

9.1.4 The following explanations are taken from Fitch's website.

9.1.5 Short and long-term credit ratings may be assigned to entities for certain sectors, including corporate, financial institutions and sovereign entities, which reflect the ability of an entity to meet financial commitments on a timely basis.

- A **short-term** issuer credit rating is based on the liquidity profile of the rated entity and relates to the ongoing capacity to meet financial obligations with a relatively short time horizon (less than 13 months) e.g. F1, F2, F3.

- A **long-term** credit rating is assigned to issuers and counterparties reflecting their ability to meet all of their most senior financial obligations on a timely basis over the term of the obligation e.g. AA, A, BBB.

9.1.6 Fitch also assign individual and support ratings to banks and these ratings provide a further level of assessment of entities' ability to honour its commitments.

- **Individual** ratings are assigned only to banks. These ratings attempt to assess how a bank would be viewed if it were entirely independent and could not rely on external support. These ratings are designed to assess a bank's exposure to, appetite for, and management of risk, and thus represent Fitch's view on the likelihood that it would run into significant difficulties such that it would require support e.g. A, B, C.

- **Support** ratings offer Fitch's judgement of a potential supporter's (either a sovereign state's or and institutional owner's) propensity and ability to support a bank. Its ability to support is set by the potential supporter's own Fitch long-term debt rating, thereby this rating communicates Fitch ratings' judgement on whether the bank would receive support should this become necessary e.g. 1, 2, 3.

9.1.7 The following tables set out all these credit ratings.

Long-term credit ratings

AAA	Highest credit quality. 'AAA' ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
AA	Very high credit quality. 'AA' ratings denote expectations of very low credit risk. They indicate very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A	High credit quality. 'A' ratings denote expectations of low credit risk. The capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher rates.
BBB	Good credit quality. 'BBB' ratings indicate that there are currently expectations of low credit risk. The capacity for payment of financial commitments is considered adequate but adverse changes in circumstances and economic conditions are more likely to impair this capacity. This is the lowest investment grade category.

The above are all classed as 'Investment Grade' ratings.

There are additional long-term ratings known as 'Speculative Grade', ranging from 'BB' to 'D'. A 'D' Fitch rating indicates an entity or sovereign that has defaulted on all of its financial obligations.

Short-term ratings

F1	Highest credit quality. Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.
F2	Good credit quality. A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.
F3	Fair credit quality. The capacity for timely payment of financial commitments is adequate; however, near term adverse changes could result in a reduction to non investment grade.
B	Speculative. Minimal capacity for timely payment of financial commitments, plus vulnerability to near term adverse changes in financial and economic conditions.
C	High default risk. Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon a sustained, favourable business and economic environment.
D	Indicates an entity or sovereign that has defaulted on all of its financial obligations.

Individual ratings

A	A very strong bank. Characteristics may include outstanding profitability and balance sheet integrity, franchise, management, operating environment or prospects.
B	A strong bank. There are no major concerns regarding the bank. Characteristics may include strong profitability and balance sheet integrity, franchise, management, operating environment or prospects.
C	An adequate bank, which, however, possesses one or more troublesome aspects. There may be some concerns regarding its profitability and balance sheet integrity,

	franchise, management, operating environment or prospects.
D	A bank, which has weaknesses of internal and/or external origin. There are concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects. Banks in emerging markets are necessarily faced with a greater number of potential deficiencies of external origin.
E	A bank with very serious problems, which either requires or is likely to require external support.
F	A bank that has either defaulted or, in Fitch's opinion, would have defaulted if it had not received external support. Examples of such support include state or local government support, insurance funds; acquisition by some other corporate entity or an injection of new funds from its shareholders or equivalent.

Support ratings

1	A bank for which there is an extremely high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to support the bank in question. This probability of support indicates a minimum long-term rating floor of 'A-'.
2	A bank for which there is a high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to support the bank in question. This probability of support indicates a minimum long-term rating floor of 'BBB-'.
3	A bank for which there is a moderate probability of support because of uncertainties about the ability or propensity of the potential provide of support to do so. This probability of support indicates a minimum long-term rating floor of 'BB-'.
4	A bank for which there is a limited probability of support because of significant uncertainties about the ability or propensity of the potential provide of support to do so. This probability of support indicates a minimum long-term rating floor of 'B'.
5	A bank for which external support, although possible, cannot be relied upon. This may be due to a lack of propensity to provide support or to very weak financial ability to do so. This probability of support indicates a minimum long-term rating floor of 'B-' and in many cases no floor at all.

9.2 Treasury management actions taken to reduce risks in recent months

9.2.1 The Council's initial exposure to the credit crunch came in September 2007 with the demise of Northern Rock, at that time the Council had investments totalling £13.6m with this bank and the maturity of these deposits ranged from 1 month to a year. The Government guarantee of Northern Rock though has protected the Council, however, this guarantee can be withdrawn by the Government at any time subject to only three months' notice. The treasury team has again started to place deposits with Northern Rock, but these will now only be made for less than three months to ensure they are protected by the Government guarantee.

9.2.2 The treasury team manages its counterparty risk through limits based on credit ratings. The credit rating agencies used are Fitch, Standard & Poors and Moodys – although primarily we use Fitch. The Council's credit criteria for counterparty investment purposes are contained in the annual Treasury Management Strategy, which was last approved by Cabinet Resources Committee on 25 March 2008. The demise of Northern Rock and the ongoing problems in the banking sector have meant that treasury officers have had to block certain counterparties and reduce periods of deposit with other counterparties. Of the banks previously used, Bradford & Bingley was withdrawn from the Council's counterparty list when Fitch

downgraded this bank from A to A- in June 2008; and Glitnir was also withdrawn in June 2008 when Fitch downgraded its long-term rating form 'A' to 'A-', and its short term rating from 'F1' to 'F2'.

9.2.3 In compiling the 2008/09 Treasury Management Strategy, the counterparty list was amended to reflect only the Top 12 building societies instead of the Top 20 previously.

9.2.4 Cash management has taken up significantly more time for the treasury team as a result of a number of counterparty downgrades by the credit rating agencies and the need to work harder to find suitable credit rated banks and building societies for the placement of investments.

9.2.5 The treasury team has used a combination of short-term investments using 3 month deals availing of the LIBOR margin (the difference between base rate and the LIBOR rate) and longer term Callable[1] deals to manage the Council's cash flow and core cash requirements. The minimum credit criteria used for this type of investment is AA (Fitch long-term rating), and the banks we use are Barclays, HSBC, HBOS, Royal Bank of Scotland and National Australia Bank.

9.2.6 Continuing uncertainty in the bank inter-lending market has meant that council officers are continually reacting to developments and have for some time been reducing the length of all current and future deals to periods of no longer than three months. The rating used for assessing a counterparty is proposed to be changed in the Treasury Management Strategy from Fitch long-term rating of 'A' to 'AA-', and the short-term rating from 'F1' to 'F1+'. In addition, the Fitch support rating has changed from 3 to 1 and the individual rating from 'C' to 'B'. An explanation of these ratings is outlined elsewhere in Section 9.1 of this report.

9.2.7 The treasury team has also opened a number of Instant Notice accounts with banks for immediate liquidity purposes achieving a rate of 25 to 42 basis points above base rate. These instant notice accounts allow treasury officers immediate access to funds.

9.2.8 Attached at Appendix A is an updated counterparty rating including Moodys ratings in addition to the Fitch Individual and Support ratings. Previously, the list only showed Fitch short and long term credit ratings.

9.3 Summary of support to banks being provided by governments

9.3.1 The following is a list of the guarantees provided by states where the Council has deposits invested, collated from a mixture of Government websites and market briefings.

<u>Belgium</u>

The Council has one deposit with a Belgium bank and this is with Irish Intercontinental Bank, whose parent company is KBC Bank, a Belgium bank. The

[1] Callable deposits pay a fixed rate of interest for a number of years but can be repaid by the borrower (bank) after a period of time set out in the deposit agreement (e.g. a year or other defined period of time).

credit rating of this bank is currently Fitch long-term 'AA-', short-term 'F1+', individual 'B', and support '2'.

Counterparty	£	Start	Maturity
Irish Intercontinental	7,000,000	18-Sep-08	31-Oct-08

The Belgium Government has offered to guarantee the wholesale funding of Belgium credit institutions. The guarantee is available to Belgian credit institutions that so wish, subject to a satisfactory assessment of their solvency by the Belgium Government and regulator. The guarantee covers transactions entered into or rolled over between 8 October 2008 and 31 October 2009, and that its maturity is not beyond 31 October 2011. Further details can be found by going to the following link.

http://www.lachambre.be/flwb/pdf/52/1470/52k1470001.pdf

Germany

The Council has three deposits with a German bank totalling £7.2m and these are with Depfa Bank, whose parent company is Eurohypo Bank, a German bank. The credit rating of this bank is currently Fitch long-term 'A-', short-term 'F1', individual 'F', and support '1'.

Counterparty	£	Start	Maturity
Depfa Bank	3,000,000	30-May-08	28-Nov-08
Depfa Bank	2,200,000	20-Aug-08	01-Dec-08
Depfa Bank	2,000,000	07-Feb-08	07-Nov-08

Legislation has been ratified by the two houses of the German parliament, the Bundestag and the Bundesrat; government guarantees worth more than 400 billion euros are available to re-launch inter-bank lending. In addition to this sum, the German government is willing to recapitalise banks up to a ceiling of 80 billion euros, provided strict conditions are met, and it will buy up difficult loans. The new package is intended to generate new confidence on the markets, Chancellor Angela Merkel announced.

Federal President Horst Köhler signed the Financial Market Stabilisation Law on 17 October 2008, shortly after it was endorsed by the Bundestag and the Bundesrat. On Saturday 18 October 2008 it will come into effect. On Monday 20 October 2008 the German Cabinet will adopt the ordinance required to put the provisions of the law into practice, and the capital will then be available to banks requiring assistance.

http://www.bundesregierung.de/Content/EN/Artikel/2008/10/2008-10-13-finanzmarktgesetz__en.html

Ireland

The Council has various deposits with Irish banks totalling £52.2m, three of which are Instant Notice accounts that allow immediate withdrawal of funds on the day.

Counterparty	£	Start	Maturity
Allied Irish Bank (instant access)	12,000,000	24-Aug-07	Call
Anglo Irish Bank	2,750,000	25-Jun-08	18-Mar-09
Anglo Irish Bank (instant access)	250,000	14-Feb-06	Call

Bank Of Ireland (instant access)	9,000,000	03-Sep-08	Call
Bank Of Ireland	5,000,000	10-Sep-08	31-Oct-08
Bank Of Ireland	1,000,000	09-Jul-08	31-Oct-08
Ebs	5,000,000	05-Feb-08	05-Nov-08
Ebs	4,000,000	05-Sep-08	19-Dec-08
Irish Nationwide	6,200,000	01-Oct-08	01-Apr-09
Irish Nationwide	5,000,000	06-Oct-08	27-Feb-09
Irish Nationwide	2,000,000	06-Feb-08	06-Nov-08

The Irish Government has decided to put in place with immediate effect a guarantee arrangement to safeguard all deposits (retail, commercial, institutional and interbank), covered bonds, senior debt and dated subordinated debt (lower tier II), with the following banks:- Allied Irish Bank, Bank of Ireland, Anglo Irish Bank, Irish Life and Permanent, Irish Nationwide Building Society and the Educational Building Society and such specific subsidiaries as may be approved by Government following consultation with the Central Bank and the Financial Regulator.

It has done so following advice from the Governor of its Central Bank and the Financial Regulator about the impact of the recent international market turmoil on the Irish Banking system. The guarantee is being provided at a charge to the institutions concerned and will be subject to specific terms and conditions so that the taxpayers' interest can be protected. The guarantee will cover all existing aforementioned facilities with these institutions and any new such facilities issued from midnight on 29 September 2008, and in both instances the cover only applies to deposits that will expire at midnight on 28 September 2010.

The decision has been taken by the Government to remove any uncertainty on the part of counterparties and customers of the six credit institutions. Its objective in taking this decisive action is to maintain financial stability for the benefit of depositors and businesses and is in the best interests of the Irish economy.

This guarantee covers in the region of €600 billion of senior obligations, compared to the GDP of Ireland which currently stands at around €175 billion. Up until yesterday, however, there were nonetheless some concerns in the market about how robust this guarantee would be in practice. When the guarantee was introduced a large volume of funds flowed from UK banks to their Irish equivalents. Following the strong implicit support offered by the UK government for the UK banks, this flow of funds may reverse, so it is possible to envisage a situation where this might de-stabilise the Irish banks. In addition, the Irish banks have a heavy exposure to the property market in the UK and Ireland which is expected to weaken their capital base over the coming months.

Clearly sensing this market view, the Irish Government last night announced further details of its guarantee package, which are attached at Appendix B. The first sentence of the statement is slightly ambiguous in regards to the dates quoted, but this has been checked with the external treasury advisors and the response is that the guarantee covers deposits maturing in the period 30 September 2008 to 29 September 2010. The committee may feel that this guarantee strengthens the security of the council's deposits in Ireland and that we should continue to place money there, but obviously within the defined maturity period and at less than three months notice.

http://www.centralbank.ie/frame_main.asp?pg=results.asp

Saudi Arabia

The Council has five deposits with two Saudi Arabian banks totalling £25m. The credit rating of Arab National bank is Fitch long-term 'A', short-term 'F1', individual 'B', and support '1'. The credit rating of Riyad bank is Fitch long-term 'A+', short-term 'F1', individual 'B', and support '1'

Counterparty	£	Start	Maturity
Arab National Bank	6,500,000	08-Sep-08	31-Dec-08
Arab National Bank	2,500,000	11-Aug-08	27-Oct-08
Arab National Bank	1,000,000	31-Jul-08	31-Oct-08
Riyad Bank	12,000,000	14-Jul-08	28-Nov-08
Riyad Bank	3,000,000	15-Jul-08	15-Jan-09

The Central Bank of Saudi Arabia has not made any explicit guarantee of wholesale deposits, however, the Central bank has made available $40bn for its banks.

http://www.sama.gov.sa/en/news/2008-10/speech_of_his_excellency_the_governor_44.pdf

United Arab Emirates

The Council has three deposits with the National Bank of Abu Dhabi totalling £9.8m. The credit rating of National bank of Abu Dhabi is Fitch long-term 'AA-', short-term 'F1+', individual 'B', and support '1'.

Counterparty	£	Start	Maturity
National Bank Of Abu Dhabi	5,000,000	17-Mar-08	17-Mar-09
National Bank Of Abu Dhabi	3,500,000	03-Jul-08	31-Oct-08
National Bank Of Abu Dhabi	1,300,000	09-Sep-08	07-Jan-09

The United Arab Emirates has guaranteed all deposits with local banks, including the country's two largest lenders Emirates NBD and National Bank of Abu Dhabi, to ensure that credit continues to flow.

The measure, which also includes a guarantee of all inter- bank lending in the U.A.E., is designed to "ensure continuity of economic growth and protect the national economy," state-owned Emirates News Agency reported, citing Prime Minister Sheikh Mohammed bin Rashid Al-Maktoum. The links below come from the official website of the central bank of the United Arab Emirates.

http://www.centralbank.ae/pdf/Releases/pressRel11-10-2008.pdf

http://www.centralbank.ae/pdf/Releases/pressRel22-09-2008.pdf

http://www.centralbank.ae/pdf/Releases/pressRel18-09-2008.pdf

United Kingdom

The UK Government has established a facility which will allow the Government to make available Tier 1 capital in the form of either preference shares or Permanent Interest Bearing Shares (PIBS) for eligible institutions named as:

- Abbey
- Barclays
- HBOS

- HSBC
- Lloyds TSB
- Nationwide Building Society
- Royal Bank of Scotland
- Standard Chartered

(other institutions may still apply).

Specifically, the Government will make available to these eligible institutions for an interim period, a Government guarantee of any new short and medium term debt issuance within the wholesale lending markets and does not include a guarantee over all deposits from investors. To qualify for this support, relevant institutions must raise Tier 1 capital by an appropriate amount and have access to a £25bn credit line to enable them to do so. Once this has been achieved, relevant institutions will be allowed to dip into the £250bn pot of cash that has now been made available.

This guarantee over interbank lending should be seen as a positive sign in the markets as it will provide confidence to the wholesale market to lend to each other once again. The consequence of such a move should see LIBOR rates reduce from these elevated levels as cash begins to move around the system once more.

http://www.bankofengland.co.uk/publications/news/2008/066.htm

Summary

The Council has a number of overseas deposits with banks totalling £101.2m excluding the investments it holds with the Icelandic banks totalling £27.4m. All of these deposits in Belgium, Germany, Ireland, Saudi Arabia and the United Arab Emirates are due to mature by 1 April 2009. The only non-UK deposit to mature after 1 April 2009 is the £15m deposit with Landisbanki. The above guarantees either explicit in the case of Saudi Arabia or implicit by the other sovereign governments indicate the level of support these governments are prepared to give during this period of instability in the financial markets.

Council officers will reduce the council's exposure to overseas markets by depositing future maturing deposits in the United Kingdom and Ireland. However, in the case of Ireland this exposure will be reduced and any further deposits will be for periods of no greater than three months. In addition, officers will try to negotiate directly with these overseas banks to exit deposits that have not matured. However, current indications are that these banks are unwilling to break these deposits and if so will make punitive charges. IS THREE MONTHS TOO LONG?

9.4 Update on recovery of deposits in Icelandic banks

9.4.1 It is very difficult to establish at the present time what the total liabilities of the Icelandic banks are and the asset cover for their liabilities. Largely all we do know is that the UK Government used anti-terrorism laws to seize the assets of Landisbanki in the UK that are believed to be around £4bn, and that the outstanding sums due to 300,000 Icesaver account holders are estimated at £3bn. The UK Treasury is putting together a plan to lend about £3bn to Iceland so it can repay the UK depositors in Icesave, and the Icelandic Government has entered into negotiations with the International

Monetary Fund (IMF) to obtain funding reputed to be £3.5bn.

9.5 Further amendments to the Treasury Management Strategy 2008-09

9.5.1 The table at the end of this section shows the current and proposed new limits for placing deposits with counterparties, and replaces that included in the report circulated with the agenda. This table now includes the full set of credit, individual and support ratings.

9.5.2 In respect to building societies it currently only includes Nationwide, given that this is the largest one and was expressly mentioned in the UK Treasury guarantee announcements, and that only today (23 October 2008) Barnsley BS announced merger talks with Yorkshire BS to address a previously undisclosed £10m exposure to Icelandic banks. However, if the crisis worsens and we have to limiting our deposits to UK banks only, then the counterparty limit of £25m would be insufficient to cover our cash balances. Given this potential scenario, Members might want to consider including the Top 5 building societies in the counterparty list at this time – these being Britannia, Yorkshire, Coventry and Chelsea in addition to Nationwide. If Members do include the remainder of the Top 5, a counterparty limit of £10m to £15m might be appropriate.

	Current	Proposed
Credit rating	Fitch long-term rating **A** Fitch short-term rating **F1** Fitch Individual rating **C** Fitch Support **3** or Moodys and Standard & Poors equivalent ratings. **Top 12 building societies** as per the Building Societies Association asset list.	Fitch long-term rating **AA-** Fitch short-term rating **F1+** Fitch Individual rating **B** Fitch Support rating **1** or Moodys and Standard & Poors equivalent rating. **Nationwide Building Society**
Counterparty limit	**£15m** (banks and Top 5 building societies) **£10m** (Top 6-12 building societies) **£15m** (UK Government [e.g. gilts and Debt Management Office Deposit Account], Local Authorities, Supranational Institutions [e.g. World Bank]).	**£25m** (banks and Nationwide Building Society) - **£25m** (UK Government [e.g. gilts and Debt Management Office Deposit Account], Local Authorities, Supranational Institutions [e.g. World Bank]).

10. LIST OF BACKGROUND PAPERS

10.1 Various market briefings.

Legal: JEL
CFO: CM/JB

Counterparty name	£	Start	Maturity	Fitch rating								Moodys						Comment
				At Time of Deposit				Current				At Time of Deposit			Current			
				Long	Short	Individual	Support	Long	Short	Individual	Support	Long	Short	FSR	Long	Short	FSR	
ABBEY	1,600,000	20-Aug-08	Instant access	AA-	F1+	B	2	AA-	F1+	B	2	Aa3	P-1	C+	Aa3	P-1	C+	
ALLIANCE & LEICESTER	4,200,000	26-Aug-08	26-Nov-08	A+	F1	B	3	A+	F1	B	3	A1	P-1	C+	A1	P-1	C+	
	1,700,000	10-Sep-08	10-Dec-08	A+	F1	B	3	A+	F1	B	3	A1	P-1	C+	A1	P-1	C+	
	3,000,000	21-Jan-08	21-Jan-09	AA-	F1+	B	3	A+	F1	B	3	Aa3	P-1	B-	A1	P-1	C+	
ALLIED IRISH BANK	12,000,000	24-Aug-07	Instant access	AA-	F1+	B	1	AA-	F1+	B	1	Aa2	P-1	B-	Aa2	P-1	B-	
ANGLO IRISH BANK	2,750,000	25-Jun-08	18-Mar-09	A+	F1	B	3	A+	F1+	B	3	A1	P-1	C+	A1	P-1	C+	
	250,000	14-Feb-06	Instant access	A	F1	B	3	A+	F1+	B	3	A2	P-1	C+	A1	P-1	C+	
ARAB NATIONAL BANK	2,500,000	11-Aug-08	27-Oct-08	A	F1	B	1	A	F1	B	1	A1	P-1	C	A1	P-1	C	
	1,000,000	31-Jul-08	31-Oct-08	A	F1	B	2	A	F1	B	1	A1	P-1	C	A1	P-1	C	
	6,500,000	08-Sep-08	31-Dec-08	A	F1	B	1	A	F1	B	1	A1	P-1	C	A1	P-1	C	
BANK OF IRELAND	1,000,000	09-Jul-08	31-Oct-08	AA-	F1+	B	1	AA-	F1+	B	1	Aa2	P-1	B-	Aa2	P-1	B-	
	5,000,000	10-Sep-08	31-Oct-08	AA-	F1+	B	1	AA-	F1+	B	1	Aa2	P-1	B-	Aa2	P-1	B-	
	9,000,000	03-Sep-08	Instant access	AA-	F1+	B	1	AA-	F1+	B	1	Aa2	P-1	B-	Aa2	P-1	B-	
BANK OF SCOTLAND - IRELAND	4,000,000	02-Jul-08	31-Oct-08	AA+	F1+	A/B	1	AA	F1+	B	1	Aa1	P-1	B	Aa1	P-1	B	
	11,000,000	14-Jul-08	14-Jul-09	AA+	F1+	A/B	1	AA	F1+	B	1	Aa1	P-1	B	Aa1	P-1	B	
BARCLAYS	5,000,000	17-Oct-08	17-Dec-08	AA	F1+	A/B	1	AA	F1+	A/B	1	Aa1	P-1	B	Aa1	P-1	B	
BARCLAYS - callable deposit	7,000,000	07-Mar-08	07-Mar-13	AA+	F1+	A/B	1	AA	F1+	A/B	1	Aa1	P-1	B+	Aa1	P-1	B	
BRADFORD AND BINGLEY PLC	2,200,000	30-May-08	28-Nov-08	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-2	C	n/a	n/a	n/a	Removed from Sector listing, guaranteed 3 months
Britannia BS	2,800,000	08-Jul-08	31-Oct-08	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C+	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	2,000,000	20-Aug-08	01-Dec-08	A	F1	B/C	3	n/a	n/a	n/a	n/a	A2	P-1	C+	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	5,000,000	11-Sep-08	02-Jan-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	1,500,000	06-Jun-08	08-Jun-09	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C+	n/a	n/a	n/a	
CATER ALLEN BANK	10,000,000	04-Aug-08	04-Aug-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Removed from Sector listing, linked to Abbey
Chelsea Building Soc.	2,000,000	31-Jul-08	31-Oct-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	10,000,000	08-Sep-08	08-Dec-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	1,500,000	08-Sep-08	08-Dec-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
Cheshire BS	2,300,000	07-Aug-08	07-Nov-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	3,000,000	05-Sep-08	19-Dec-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	4,000,000	22-Sep-08	23-Dec-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
Coventry Building Soc.	1,500,000	03-Jul-08	31-Oct-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	8,100,000	15-Sep-08	30-Jan-09	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	3,000,000	17-Sep-08	30-Jan-09	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	2,000,000	21-May-08	21-May-09	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
DEPFA BANK	2,000,000	07-Feb-08	07-Nov-08	A	F1	N/R	2	A-	F1	N/R	1	Aa3	P-1	C+	A2	P-1	D+	
	3,000,000	30-May-08	28-Nov-08	A	F1	N/R	2	A-	F1	N/R	1	Aa3	P-1	C+	A2	P-1	D+	
	2,200,000	20-Aug-08	01-Dec-08	A	F1	N/R	2	A-	F1	N/R	1	Aa3	P-1	C+	A2	P-1	D+	
Derbyshire BS	2,000,000	07-Aug-08	07-Nov-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	2,600,000	05-Sep-08	01-Dec-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	5,000,000	08-Sep-08	08-Dec-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
EBS	5,000,000	05-Feb-08	05-Nov-08	A	F1	B	3	A	F1+	B	3	A1	P-1	C+	A1	P-1	C+	
	4,000,000	05-Sep-08	19-Dec-08	A	F1	B	3	A	F1+	B	3	A1	P-1	C+	A1	P-1	C+	
Glasgow City Council	2,500,000	21-Oct-08	24-Oct-08	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Local Authority
GLITNER BANK (ICELAND)	7,000,000	07-Nov-06	07-Nov-08	A	F1	B/C	2	n/a	n/a	n/a	n/a	A1	P-1	C+	n/a	n/a	n/a	Removed from Sector listing
	2,400,000	07-Feb-07	09-Feb-09	A	F1	B/C	2	n/a	n/a	n/a	n/a	A1	P-1	C+	n/a	n/a	n/a	Removed from Sector listing
	3,000,000	24-Jan-07	24-Mar-09	A	F1	B/C	2	n/a	n/a	n/a	n/a	A1	P-1	C+	n/a	n/a	n/a	Removed from Sector listing
HBOS - callable deposit	5,000,000	29-May-07	29-May-12	AA+	F1+	A/B	1	AA	F1+	B	1	Aa2	P-1	n/a	Aa1	P-1	n/a	
HSBC - callable deposit	5,000,000	21-Apr-08	19-Apr-13	AA	F1+	A/B	1	AA	F1+	A/B	1	Aa1	P-1	B	Aa1	P-1	B	
IRISH INTERCONTINENTAL	7,000,000	18-Sep-08	31-Oct-08	A+	F1	B	1	A+	F1	B	1	A1	P-1	C	A1	P-1	C	
IRISH NATIONWIDE	2,000,000	06-Feb-08	06-Nov-08	A	F1	B	3	n/a	n/a	n/a	n/a	A3	P-2	C-	n/a	n/a	n/a	Removed from Sector listing
	5,000,000	06-Oct-08	27-Feb-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Irish State guarantee
	6,200,000	01-Oct-08	01-Apr-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Irish State guarantee
LANDISBANKI ISLANDS H.F.	15,000,000	28-Sep-07	28-Sep-10	A	F1	B/C	2	BBB	F3	C	2	Aa3	P-1	C	A2	P-1	C-	
Leeds BS	2,800,000	20-Aug-08	26-Nov-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	2,500,000	21-Aug-08	26-Nov-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	2,500,000	29-Sep-08	30-Jan-09	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
NATIONAL BANK OF ABU DHABI	3,500,000	03-Jul-08	31-Oct-08	AA-	F1+	B/C	1	AA-	F1+	B/C	1	Aa3	P-1	C	Aa3	P-1	C	
	1,300,000	09-Sep-08	07-Jan-09	AA-	F1+	B/C	1	AA-	F1+	B/C	1	Aaa3	P-1	C	Aa3	P-1	C	
	5,000,000	17-Mar-08	17-Mar-09	AA-	F1+	B/C	1	AA-	F1+	B/C	1	Aa3	P-1	C	Aa3	P-1	C	
Nationwide BS	10,500,000	15-Oct-08	24-Nov-08	AA-	F1+	A/B	2	AA-	F1+	A/B	2	Aa2	P-1	B	Aa2	P-1	B	
	1,500,000	15-Jul-08	15-Jan-09	A	F1	B	3	AA-	F1+	A/B	2	A2	P-1	C	Aa2	P-1	B	
Newcastle Building Soc.	2,000,000	02-Oct-08	06-Feb-09	A	F1	B	3	A	F1	B	3	A2	P-1	C	A2	P-1	C	
	3,000,000	02-Oct-08	27-Feb-09	A	F1	B	3	A	F1	B	3	A2	P-1	C	A2	P-1	C	
Northern Rock plc	11,000,000	15-Oct-08	13-Jan-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	HM Government guaranteed 3 months
Principality Building Soc.	1,000,000	20-Aug-08	01-Dec-08	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C+	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	2,500,000	16-Apr-08	16-Jan-09	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C+	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	2,500,000	29-Sep-08	30-Jan-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	4,000,000	02-Oct-08	30-Jan-09	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	Building Societies included in Treasury Strategy
RIYAD BANK	12,000,000	14-Jul-08	28-Nov-08	A	F1	B	1	A+	F1	B	1	A1	P-1	C	A1	P-1	C	
	3,000,000	15-Jul-08	15-Jan-09	A	F1	B	1	A+	F1	B	1	A1	P-1	C	A1	P-1	C	
RBS - callable deposit	5,000,000	25-May-07	25-May-11	AA+	F1+	A/B	1	AA	F1+	A/B	1	Aaa	P-1	B+	Aa1	P-1	B	
	5,000,000	17-Jun-08	17-Jun-13	AA	F1+	A/B	1	AA	F1+	A/B	1	Aaa	P-1	B+	Aa1	P-1	B	
Skipton BS	5,000,000	08-Aug-08	24-Nov-08	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
	3,000,000	29-May-08	29-May-09	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C+	
West Bromwich BS	3,000,000	10-Jul-08	31-Oct-08	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C	n/a	n/a	n/a	Building Societies included in Treasury Strategy
	3,000,000	03-Jul-08	05-Jan-09	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C	n/a	n/a	n/a	Building Societies included in Treasury Strategy
West Bromwich BS	3,600,000	19-Jun-08	18-Jun-09	A	F1	B	3	n/a	n/a	n/a	n/a	A2	P-1	C	n/a	n/a	n/a	Building Societies included in Treasury Strategy
Yorkshire BS	3,000,000	09-Jul-08	31-Oct-08	A+	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C	
	10,000,000	15-Jul-08	23-Dec-08	A+	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C	
	2,000,000	17-Sep-08	30-Jan-09	A	F1	B	3	A	F1	B	3	A2	P-1	C+	A2	P-1	C	
	337,500,000																	

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Credit Institutions (Financial Support) Scheme 2008 (the "Scheme")

Market Notice - Confirmation of Statutory Guarantee

1. Nature of the statutory guarantee

The covered liabilities of participating covered institutions for the period 30 September 2008 to 29 September 2010 inclusive are guaranteed under the laws of Ireland by the Minister for Finance.

In the event of any default of a covered institution in respect of a covered liability, the Minister for Finance will pay to the relevant creditor, on demand, an amount equal to the unpaid covered liabilities.

The guarantee is unconditional and irrevocable and ensures timely payment of the covered liabilities of the covered institutions.

Should a covered institution be removed from the Scheme, all of its fixed term covered liabilities outstanding at that time will continue to have the full benefit of the guarantee to 29 September 2010 or their maturity, whichever is the earlier. All covered liabilities, including on-demand deposits, will be protected by notice of at least 90 days prior to any covered institution being removed from the Scheme.

No call can be made under the guarantee after 29 September 2010.

The guarantee does not affect any other rights or claims of creditors.

2. Designation of covered institutions

The Minister for Finance will make an order designating the credit institutions (which for the avoidance of doubt includes any of their branches) and named subsidiaries that will be able to join the Scheme.

In order to join the Scheme these institutions will be required to execute a "guarantee acceptance deed". Institutions that join the Scheme will become "covered institutions".

Once it has executed a guarantee acceptance deed and the Minister has made the requisite order, the name of each covered institution will be published on the website of the Department of Finance http://www.financegov.ie .

3. Covered liabilities

The following liabilities are covered by the Scheme ("covered liabilities"):

- all retail and corporate deposits (to the extent not covered by existing deposit protection schemes in Ireland or any other jurisdiction);
- interbank deposits;
- senior unsecured debt;
- covered bonds (including asset covered securities); and
- dated subordinated debt (Lower Tier 2).

4. Risk weighting

The Financial Regulator has deemed that, under the Standardised Approach, covered liabilities would qualify for zero risk weighting for capital adequacy purposes during the period of the guarantee.

5. Charge and indemnity

The covered institutions will pay a quarterly charge to the Exchequer for the guarantee. The aggregate amount of the charge is based on the increased debt servicing costs that the State bears as a result of providing the guarantee. Current estimates are that over the two years of the Scheme the charge to the covered institutions for the guarantee will yield €1bn.

By joining the Scheme, a covered institution will also agree to indemnify the Minister in respect of any payments made, or costs incurred, by the Minister in respect of the guarantee relating to that covered institution.

A covered institution is not required to indemnify the Minister in respect of any payments made by the Minister under a guarantee given to any other covered institution which is not a member of its corporate group.

6. Legislative Basis

Under the Credit Institutions (Financial Support) Act 2008 (the "Act"), the Minister for Finance has the power to provide guarantees to covered institutions.

The Scheme, which provides for the terms and conditions under which the guarantee is provided, was approved by both Houses of the Oireachtas (i.e. the Irish Parliament) on 17 October 2008.

The Act, the Scheme and Ministerial orders made under section 6(1) of the Act provide the statutory basis to the credit institution guarantee arrangement announced by the Minister for Finance on 30 September 2008 and 9 October 2008.

The Scheme has been approved by the European Commission as being compatible with EC Treaty State aid rules.

Further information

A copy of the Act and the Scheme are available on the Department of Finance website: http://www.finance.gov.ie

Department of Finance
22 October 2008