

LAAP bulletin 82

guidance on the impairment of deposits with Icelandic Banks

Update No. 7

May 2013

The Local Authority Accounting Panel issues LAAP Bulletins to assist practitioners with the application of the requirements of the Code of Practice on Local Authority Accounting, SeRCOP and Prudential Code, and to provide advice on emerging or urgent accounting issues. Bulletins provide influential guidance that is intended to be best practice, but are not prescriptive and do not have the formal status of the Code, SeRCOP or Prudential Code.

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BACKGROUND

1. LAAP Bulletin 82 provided advice on estimating the impairments to be recognised in relation to deposits in Icelandic banks. This guidance was based on published information at the date the bulletin was issued, and since then five updates have been issued. The last update was issued in May 2012. Since that date, further information has become available. This update sets out the position at May 2013 and provides advice on estimating the impairments based on the latest position.
2. The Code requires the Statement of Accounts to be adjusted for events that occur after the balance sheet date, and which provide evidence of conditions that existed at the Balance Sheet date:

3.8.2.1 Events after the reporting period are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. Two types of events can be identified:

- a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period), and*
- b) Those that are indicative of conditions that arose after the reporting period (non-adjusting events after the reporting period).*

3.8.4.1 An authority shall disclose the following:

...

- 2) If an authority receives information after the reporting period, but before the financial statements are authorised for issue, about conditions that existed at the end of the reporting period, the authority shall update disclosures that relate to these conditions, in the light of the new information.*

...

3. However, the Statement of Accounts need not be adjusted for immaterial amounts:

2.1.2.7 ... An authority need not comply with the Code, as to both disclosure and accounting principles, if the information is not material to the true and fair view of the financial statements and to the understanding of users.

4. The amounts to be recognised in the accounts in respect of the value of the deposits, and the impairments to be charged to the Comprehensive Income and Expenditure Statement are accounting estimates.
5. The spreadsheet accompanying this Bulletin has been amended to reflect the recommended treatment and it should be noted that there are now three separate sheets, one for Heritable Bank plc and Kaupthing Singer & Friedlander Ltd, and separate ones for Glintrir and Landsbanki.

UPDATED ESTIMATES

6. The following paragraphs set out the latest information in respect of each bank.

Heritable Bank plc

7. At the time LAAP Bulletin 82 Update 6 was issued, the total amount to be received was estimated to be between 86% and 90% of the claim. Since then the twelfth interim payment was made in July 2012 and was for 2.85% of the claim and the thirteenth interim payment was made in January 2013 and was for 2.72% of the claim. Total recoveries to date therefore total 77.2% of the claim. The Administrators latest

estimate of total recoveries remains 86% to 90% of the claim. However it is understood that Heritable's residential mortgage book, which constituted the largest asset remaining in the Administration, was sold to a third party on 15 May 2013. This is likely to impact the amount and profile of future recoveries and authorities may need to make further adjustments to the profile of repayments after the Administrators have been able to provide a more detailed update. In relation to any changes to the estimated amount and profile of future recoveries, authorities should have regard to paragraphs 2 and 3 in this Bulletin which relate to events after the balance sheet date and materiality. LAAP will, if appropriate, issue an amended recommendation in due course.

8. In view of the above information, LAAP currently recommends the estimate of the recoverable amount is based on a total repayment of 88% based on the mid-point of the base case return and that subsequent repayments are profiled as follows:

Date	Repayment	Date	Repayment
July 2013	2.00%	January 2014	8.80%

Kaupthing Singer & Friedlander Ltd

9. At the time LAAP Bulletin 82 Update 6 was issued, the total amount to be received was estimated to be between 81% and 86% of the claim. The estimated recoverable amount was the mid-point 83.5%. Since then, the ninth dividend, 3% of the claim, was paid on 31 October 2012. This brought the total recoveries to 76% of the claim. The Administrators' Progress report to creditors for the six month period from 8 April 2012 to 7 October 2012¹ estimated that the total amount to be received was 84% to 86.5% and this estimate has been maintained in the report just issued covering the period to 7 April 2013. On 29 April 2013, the Administrators announced that they would pay a dividend of not less than 2% of the claim in the week commencing 3 June 2013.

10. In view of the above information, LAAP recommends the estimate of the recoverable amount is at the mid-point, which is now 85.25%. An appropriate estimate for the payment schedule is considered to be:

Date	Repayment	Date	Repayment
June 2013	2.00%	June 2014	3.50%
June 2015	3.75%		

Iceland-domiciled banks

Glitnir Bank hf

11. After the decision of the Icelandic Supreme Court had been delivered, the Winding Up Board of Glitnir made a distribution proposal to priority creditors. This was accepted by all UK local authorities and implemented on 16 March 2012. Under the terms of the distribution proposal, payment of each depositor's claim (measured in ISK terms as at 22 April 2009) was made in a basket of currencies with conversions made using Central Bank of Iceland selling rates as at 22 April 2009. The distribution currencies were Icelandic kroner, Euros, US dollars, pounds sterling, and Norwegian krona. The weightings for the distribution currencies were determined based on the currencies of the adjusted assets held by Glitnir as at 30 September 2011.

12. The ISK amounts that have been distributed by the Glitnir Winding Up Board are held in escrow because, under the applicable currency controls operating in Iceland, the

¹ http://www.kaupthingsingers.co.uk/media/1558/progress_report_oct_2012.pdf

permission of the Central Bank of Iceland is required to release Icelandic kroner payments held within the Icelandic banking system². The money held in the Glitnir Winding Up Board escrow account is, however, still earning interest for the benefit of local authorities at a rate of 3.4% up to 22 June 2012 and at 4.2% from 22 June 2012. Whilst this was not an arm's length transaction, the interest rate appears to reflect market rates in Iceland and hence there is no requirement to use a different discount rate. Given that the money held is not readily convertible to known amounts of cash it is not recommended that the sum is treated as a cash equivalent. The Icelandic kroner element of the Glitnir distribution to UK local authorities should therefore continue to be considered to be an investment that should be accounted for in its own right. It will be for each authority to decide whether it should classify the investment as short or long term based upon its own plans. Accruing interest should be credited to the Comprehensive Income & Expenditure Statement and any foreign exchange difference arising at 31 March 2013 (£1 = 188.97 ISK) reflecting changes in the Central Bank of Iceland selling rate should also be taken to the Comprehensive Income and Expenditure Statement.

LBI hf (formerly Landsbanki Islands hf)

13. At the time LAAP Bulletin 82 Update 6 was issued, the total payment was estimated to be 100%. Since the last Bulletin a sterling distribution was made on 24 May 2012, representing 12.32% of the total (using 22 April 2009 exchange rates). A further distribution of sterling, US Dollars and Euro were made on 5 October 2012, representing 6.2% of the total (at 22 April 2009 exchange rates).
14. The Winding Up Board published details of LBI's financial position as at 31 December 2012 on its website³. This showed that LBI's assets, including partial payments already made in respect of priority claims were greater than the sum of the priority claims. It is therefore still considered likely that UK local authorities will recover 100% of their deposits, subject to potential future exchange rate fluctuations.
15. There is an on-going dispute over whether the total claims should be valued at the 22 April 2009 exchange rates or at spot rates. This is being trialled in the Icelandic Courts shortly and is likely to be the subject of appeal to the Icelandic Supreme Court whatever the verdict. For the purposes of this Bulletin, the use of the 22 April 2009 exchange rates have been assumed as this is more prudent.
16. The future pattern of distributions by the Landsbanki Winding Up Board is not known, but based on the above information and an estimate that the distribution made in October 2012 represented 49.65% of the total due (based on the 22 April 2009 exchange rates), LAAP recommends that the estimate of the recoverable amount is based on a total repayment of 100% and that the future payment schedule should be estimated as follows:

Date	Repayment	Date	Repayment
December 2013	7.50%	December 2017	7.50%
December 2014	7.50%	December 2018	7.50%
December 2015	7.50%	December 2019	5.35%
December 2016	7.50%		

² see the Central Bank of Iceland announcement at <http://www.sedlabanki.is/?PageID=287&NewsID=3123>

³ <http://www.lbi.is/home/winding-up-proceedings/financial-information/>

17. As with Glitnir, Icelandic kroner distributions already made to authorities have been placed into escrow which should continue to be treated as either a short or long term investment. This is earning interest at the following rates for 2012/13:

1 April 2012 to 20 May 2012	3.59%
21 May 2012 to 20 June 2012	3.93%
21 June 2012 to 31 March 2013	4.17%

18. This interest should be accrued and credited to the Comprehensive Income and Expenditure Statement. Authorities should account for an exchange difference based on the ISK exchange rate at 31 March 2013 (£1 = 188.97 ISK) as against that as at 31 March 2012 (£1 = 202.95 ISK) in respect of the change in value of the ISK element of their distribution, which should also be taken to the Comprehensive Income and Expenditure Statement.