

A REPORT BY THE AUDITOR GENERAL FOR SCOTLAND UNDER SECTION 22(3)
OF THE PUBLIC FINANCE AND ACCOUNTABILITY (SCOTLAND) ACT 2000

THE 2008/2009 AUDIT OF THE ROYAL BOTANIC GARDEN EDINBURGH

1. I have received the audited accounts of the Royal Botanic Garden Edinburgh (RBGE) for the year ended 31 March 2009. The auditors' report on the accounts is not qualified but I have prepared this report to draw the Parliament's attention to the potential loss of public funds relating to the Icelandic banking crisis.
2. I submit these accounts and the auditor's report in terms of sub-section 22(4) of the Public Finance and Accountability (Scotland) Act 2000, together with this report which I have prepared under section 22(3) of the Act.

History

3. The Trustees of the RBGE approved the opening of an account with Singer and Friedlander on 5 October 2005. The account was opened in November 2005 with an initial deposit of £33,527.
4. Kaupthing Holdings UK Ltd., the UK subsidiary of the Icelandic Kaupthing Bank, had acquired Singer and Friedlander in August 2005 and it subsequently became Kaupthing Singer and Friedlander (KSF). At the start of October 2008, RBGE had £1.09 million deposited with KSF made up of two elements:
 - £0.456 million of deferred Value Added Tax relating to RBGE's £15.7 million Gateway construction project. The Lennartz Mechanism allows organisations to defer payment of VAT on capital spend until the end of the project.
 - £0.635 million in the Board Reserve. RBGE is a non-departmental public body with charitable status. The Scottish Government allocated cash to RBGE in 2005 to correct a long standing cumulative deficit position and to enable it to carry a reserve as it was felt inappropriate that RBGE, as a charity, should show a deficit in its financial statements.
5. At the time RBGE made the initial investment in KSF, the bank was an A rated institution and remained so until a few weeks prior to being placed in administration. KSF went into administration on 8 October 2008 and RBGE's £1.09 million deposit was frozen.
6. As a wholesale depositor with KSF, RBGE was not covered by guarantees for retail deposits under the Financial Services Compensation Scheme. Neither did it qualify for small charity guarantees which covered charities with less than 50 employees and assets not exceeding £3.26 million.

7. In a letter to all KSF's creditors, including RBGE, dated 17 April 2009, KSF's Administrators (Ernst and Young LLP) stated that they "currently estimate that total distributions should be a minimum of 50p in the £". This suggests that a minimum of £0.545 million could be expected to be returned to RBGE. The Administrators' recently announced that they intended to make an initial distribution of 20p in the £ by the end of July 2009.
8. RBGE is a relatively small organisation with annual expenditure of £11.7 million. It is likely that the potential loss of funds invested with KSF will have a significant impact on aspects of RBGE's future operations.

Approval process

9. The Scottish Public Finance Manual requires public bodies such as RBGE to gain approval from the Scottish Government for the opening of a commercial bank account. RBGE did not obtain approval from the Scottish Government in 2005 for the opening of the account with Singer and Friedlander.
10. During 2008/09, RBGE's external auditors conducted a review of its treasury management arrangements. They noted that RBGE was required under the National Heritage (Scotland) Act 1985 and its Financial Memorandum to seek approval from the Scottish Government before making investments. It was not clear whether placing cash on deposit represented an investment requiring approval under the Financial Memorandum.
11. RBGE contacted the Scottish Government on 16 February 2009 to ask if it required approval to place cash on deposit. On 15 May 2009, the Scottish Government stated that once approval was obtained to open a bank account, then no further approval was required to place cash on deposit. On 26 May 2009, RBGE sought retrospective approval for all existing bank accounts in operation. This was granted by the Scottish Government on 27 May 2009.
12. RBGE has conducted an internal review of its decision to place cash on deposit with KSF. The review concluded that the collapse of KSF was "difficult if not impossible to anticipate". RBGE has subsequently made a number of changes to its treasury management arrangements.
 - Cash deposits may only be placed with the six UK clearing banks.
 - There is a £300,000 limit on cash deposits (with the exception of RBGE's main bankers - the Royal Bank of Scotland).
 - There is a monthly report on cash balances and institutional credit ratings.

13. I have asked RBGE's external auditors to monitor RBGE's progress in recovering the funds and report back to me in due course.

A handwritten signature in black ink that reads "AwtBlack". The letters are stylized and connected, with a small mark at the end of the word.

ROBERT W BLACK
Auditor General for Scotland
28 July 2009