



Falkirk Council

FALKIRK COUNCIL PENSION FUND

CASH MANAGEMENT POLICY

Chief Executive Office (Finance)

February 2014

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I. Introduction

This document sets out the guidelines through which cash operations, under the internal management of the Pension Fund, are carried out. The document is designed to complement the Pension Fund's Statement of Investment Principles.

In order for the Fund to meet its benefit obligations and undertake its daily business activities it is necessary for it to hold short term cash deposits. (For the avoidance of doubt, "short term" is considered to be a period of less than one year).

Surplus cash is normally invested with the Clydesdale Bank, the Fund's bankers and with Northern Trust, the Fund's Custodian.

Depending on the prevailing market interest rates, surplus cash may also be loaned to counterparties subject to their creditworthiness.

As cash is not recognised as a separate component within the Fund's strategic asset allocation, the Pensions Section will aim to keep cash holdings to a minimum. This will allow the greater part of any surplus monies to be fully invested by the investment managers.

Where it is necessary to hold cash, the general rule is that any surplus short term cash should be invested prudently with the following priorities:

- security of invested capital;
- liquidity of invested capital;
- optimisation of yield only after security and liquidity requirements reached.

(It should also be noted that within the terms of the Cash Management Policy, the Fund will not pool pension fund cash with any of Falkirk Council's own cash balances for the purpose of making investments).

II. Compliance

All cash management activities will be carried out in accordance with the relevant Local Government Pension Scheme (LGPS) regulations and Codes of Practice as set out by CIPFA.

The Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 require that an administering authority:

- invests any fund monies that are not immediately needed to meet benefit obligations;
- holds any pension fund monies in a separate account; and
- ensures that the separate account is maintained by an authorised deposit-taker.

CIPFA has prepared a Code of Practice for Treasury Management in Public Services. This provides guidance on areas such as risk management, decision making and analysis, corporate governance and cash flow management for day to day cash activities.

III. Risk Management

The Chief Finance Officer will be responsible for the design, implementation and monitoring of all arrangements for the control of cash management risk within the Fund. This will involve reporting to the Pensions Panel and Committee from time to time on the adequacy/suitability of control mechanisms, including, as a matter of urgency, any circumstances where there is likely to be a difficulty in the Fund achieving its cash management objectives.

The following areas have been identified as risk elements within the Fund's cash management operations:

1. **Credit and counterparty risk management**

A key objective of any cash management strategy is to ensure the security of the principal sums invested. To manage this risk, the Fund has produced an approved counterparty list (Appendix A). A counterparty is defined as a party to which the Fund will lend.

The Fund's list of approved counterparties details:

- the parties to which the Fund can lend;
- the limits to which the Fund can make deposits; and
- the maximum period of investment.

2. **Liquidity risk management**

The Fund does not anticipate being in a situation where it will be required to borrow monies in order to finance daily business activity. Nonetheless, in an emergency or unforeseen circumstance, the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulation 2010 would permit the Fund to borrow monies by way of temporary loan or overdraft if it was:

- to meet benefits due under the scheme; or
- to meet investment commitments arising from changes in the strategic investment allocation; and
- the Fund reasonably believed it could repay the sum borrowed and interest thereon within 90 days of the borrowing date.

As the Fund is in a cash positive position it will not engage in borrowing. It will instead use strong financial controls and cash flow monitoring/forecasting techniques to ensure that borrowing, whilst still an option, is not required.

3. **Interest rate risk management**

The Fund will manage its exposure to fluctuations in interest rates with a view to securing the best available interest without taking undue risk.

It will achieve this by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected and potentially advantageous changes in the level or structure of interest rates.

4. Exchange rate risk management

The Fund's internally managed cash arrangements do not involve having a significant exposure to currency fluctuations and as such no special arrangements to eliminate any foreign exchange exposure will be made. Occasionally, the Fund may be in receipt of income or incur expenditure in a non-Sterling currency. In such circumstances, conversion to Sterling or vice versa will be implemented at the earliest possible opportunity.

5. Legal and regulatory risk management

The Fund will ensure that all of its cash management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. It will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the Fund, particularly with regard to duty of care and fees charged.

The Fund recognises that future legislative or regulatory changes may impact on its cash management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the Fund.

6. Fraud, error and corruption, and contingency management

The Fund has sought to identify the circumstances which may result in loss through fraud, error, corruption or other eventualities in its cash management dealings. Accordingly, it will employ suitable control systems and procedures and will maintain effective contingency management arrangements.

A clear distinction will be made between those charged with setting cash management policies (i.e. Pensions Panel and Committee) and those who will implement and control the policies (i.e. Chief Finance Officer and Pensions Section Officers). Segregation of duties will also exist at an operational level with the roles of those involved in the preparation and authorisation of transactions being clearly defined.

7. Market risk management

The Fund will seek to ensure that its stated cash management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests, and will accordingly seek to protect itself from the effects of such fluctuations.

IV. Investment & Counterparty Choice

In determining the type of “cash” investment to be made and appropriate counterparty, the Fund will seek advice from the officers and advisers of Falkirk Council. Approval of a counterparty will depend on a combination of the party’s credit rating and the type of investment vehicle being offered.

All credit ratings and investment instruments will be monitored through the creditworthiness service provided by the Council’s own Treasury advisers. The Fund will also use market data, including negative rating watches and other publicly available information, when reviewing and monitoring its approved counterparties list.

Instruments for Investment

Subject to the limitations outlined below, the Fund may invest in any of the following instruments. The limitations include the instrument class, the maturity period (i.e. maximum length of deposit) and the amount of any transaction.

Instrument	Country	Counterparty	Maximum Limit of Investment £m	Maximum Length of Deposit
UK Treasury Bills	UK	Government	Unlimited	95 days
Current/Call Deposit Account	UK/UK subsidiary	Approved Counterparty Institution, Building Society or Local Authority	£8m per name *	Call
Notice Deposit Account	UK/UK subsidiary	Approved Counterparty Institution, Building Society or Local Authority	£5m per name *	95 days
Term Deposit Account	UK/UK subsidiary	Approved Counterparty Institution, Building Society or Local Authority	£5m per name *	95 days
AAA rated Money Market Funds		Money Market Fund subject to individual approval	£5m per name (except Northern Trust where limit is £10m)	Daily Liquidity
AAA rated Bond Funds		Bond Funds subject to individual approval	£2m per name	95 days

*Limit varies per counterparty (see approved counterparty list)

Credit Ratings

In determining the creditworthiness of a potential counterparty, the Fund will select the lowest credit rating for the counterparty from the published ratings of Fitch, Moody's and Standard & Poors and compare this against the minimum acceptable standard that the Fund has set. In other words, application of the Fund's criteria will apply to the lowest available rating for any institution.

The minimum level of acceptable credit rating for an approved counterparty is as undernoted. As the Fund's aim is to hold cash for short term periods only, the Fund will pay particular attention to the short term rating whilst also having regard to the long term rating.

	Moody	S&P	Fitch	
SHORT TERM	P-1	A-1	F1	Indicates the strongest capacity for timely payment of financial commitments within a 12 month timeframe.
LONG TERM	A2	A	A	High Credit Quality. A low expectation of credit risk with a strong capacity for timely payment of financial commitments.

Credit and Counterparty Arrangements

The Fund will only use counterparties who meet the criteria of suitability of instrument and credit rating. Counterparties that meet these requirements are considered 'Approved Counterparties'. The approved counterparties list is set out in Appendix A.

V. Operations

Cash Flow management is the key element of the Fund's cash operations. Daily cash flow monitoring/forecasting takes place and a monthly report analysing the cash position and projected balances is reviewed by the Pensions Manager.

There are four main streams to the Fund's Cash Flows. These are –

- Pensioner Payroll – Payments to pensioners made on the 15th of each month
- Pension Contributions – Receipts due by the 19th of the month after contributions have been deducted. All major employers pay on the 19th.
- Misc. Payments and Receipts – Irregular during the month and depends on demand. Can be forecasted (to some extent) e.g. Fund manager fees due in the month after a quarter end.
- Investments – Capital calls and distributions relating to the Fund's alternatives portfolio can materialise at short notice

Role of Chief Finance Officer

In terms of day to day operational activities, the Chief Finance Officer is responsible for:

- Approving institutions with suitable credit rating for inclusion on counterparty list;
- Monitoring the on-going credit-worthiness of counterparties;
- Deleting individual counterparties where credit ratings fail to match stated criteria;
- Reviewing lending limits and maturity periods of individual counterparties; and
- Authorising transactions in accordance with Council's authorised signatories practices.

Role of Pensions Section Officers

Officers are expected to comply at all time with the requirements of this document. Officers will perform the following cash management activities:

- Lending in accordance with approved Counterparty list;
- Assessment, approval and use of new financial instruments and cash management techniques;
- Managing the underlying risk associated with the Fund's immediate liabilities and surplus funds;
- Managing cash flow;
- Banking;
- Borrowing; and
- Use of external money managers.

Investment Limits

The Fund has an objective of keeping cash balances to a minimum. Where cash has to be held to enable the Fund to meet its statutory obligations, the primary aim is to ensure the security and liquidity of the principal sums. Obtaining an optimum yield is a secondary objective.

The limits placed on individual institutions are as set out on Page 10 of this document. These include the limits placed on the Fund's bank and custodian as noted below.

Clydesdale Bank - £8 million

Northern Trust - £10 million

The above should be interpreted as maximum limits rather than investment targets. Aggregate cash from the three categories should not exceed £20 million.

Investments should be made in compliance with the terms and conditions set out on Pages 5 and 6 of this document.

Short Term Breaches

It is recognised that on occasion short term breaches of the above limits may occur due to asset or manager restructuring. In such cases, the circumstances would be brought to the attention of the Chief Finance Officer and every reasonable action taken to ensure that the period of the breach was kept to a minimum. Similarly, the Fund is allowed to temporarily breach the £20 million limit if there is a clear near term investment pipeline in need of financing.

Clydesdale Bank

From June 2013, the Fund will operate a single current account with the Clydesdale Bank which earns the base rate of interest (0.5% pa – May, 2013).

As such, the Fund does not have an overdraft arrangement for its Clydesdale accounts. However, the relationship that the Council has with the Clydesdale allows an overdraft facility to be negotiated when required at favourable terms.

Clydesdale Bank will continue to be used for transactional purposes even if the bank falls below the Fund's required credit rating criteria. If this occurs balances will be minimised and maintained in an instantly accessible call account.

Northern Trust

Northern Trust are the Fund's appointed custodians. They offer specialised financial services and are responsible for safeguarding and recording the Fund's investment assets.

Cash held by Northern Trust consists of a) cash instruments held by external fund managers and b) cash arising as a result of the Fund's alternatives investment programme. Only cash

relating to the alternatives programme is deemed to be under internal management and thus covered by this policy document.

All monies that are deemed to be under internal management are automatically swept into one of Northern Trust's AAA rated money market funds, allowing balances to earn interest at minimal risk.

Where the level of cash held by Northern Trust on behalf of external Fund Managers is deemed excessive, this will be raised directly with the Managers by the Pensions Manager.

Currency

It is the Fund's policy to minimise its exposure to exchange rate risk. The Fund's cash management activities do not involve investment in foreign currency instruments. The exception to this rule will be the funding/receipt of Private Equity investments through Northern Trust. As there are regular calls and distributions of funds, foreign currency balances will only be exchanged at the end of each month. This reduces the need and the costs associated of having to purchase/sell currency to meet commitments.

Ancillary Systems

As of May 2013, Officers will use the undernoted IT systems to support the Cash Management Operations:

- Logotech – A comprehensive database providing loans administration, cash flow management and interest rate forecasting.
- Clydesdale Bank Business Online – This system is web based providing real time details of the Fund's account positions; processing electronic transfer of funds (CHAPS); Faster Payment Service (FPS); internal account transfers and interrogation of accounts.

Chief Finance Officer
February, 2014

Appendix A

Falkirk Council Pension Fund List of Approved Counterparties

Counterparty	Maximum Limit of Investment £m	Maximum Length of Deposit
<u>Banks</u>		
Clydesdale Bank	£8m	Call
Barclays Bank	£5m	95 days
HSBC	£5m	95 days
Lloyds Banking Group*	£5m	95 days
Santander UK	£5m	95 days
<u>Building Society</u>		
Nationwide	£2m	95 days
<u>Money Market Funds</u>		
AAA rated funds Northern Trust	£5m £10m	Call
<u>Bond Funds</u>		
AAA rated funds	£2m	95 days
<u>UK Local Authorities</u>		
All	£5m	95 days
<u>UK Government</u>		
	Unlimited	95 days

* Consists of Lloyds TSB and Bank of Scotland. Limit is the maximum of combined monetary value of group.