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Pension Fund Committee Distribution List

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Date: 18 January 2010

Dear Member

Pension Fund Committee Meeting 21 January 2010

Please find attached the papers for the item below. I would be grateful if you could ensure that you bring these to the meeting on Thursday. Many thanks.

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Yours sincerely

Maureen Keyworth

Maureen Keyworth
Democratic Services Officer

Agenda Item 5

Report to Pension Fund Committee

Title: **Treasury Management Service Level Agreement**

Date: **21 January 2010**

Date Decision can Be implemented: **21 January 2010**

Author: **Pensions & Investments Manager**

Contact Officer: **Julie Edwards 01296 383910**

Electoral Divisions Affected: **n/a**

Portfolio Areas Affected: **None**

Purpose of Report

To formalise the arrangements for investing the Pension Fund's surplus cash balances.

Summary

At its meeting on 19 November 2009, the Pension Fund Committee agreed that the arrangements for investing the Fund's surplus cash should be documented in a Service Level Agreement (SLA) and agreed by the Committee. This report documents the arrangements for managing the Pension Fund bank account and investment of cash.

Recommendation

The Committee is asked to APPROVE the Pension Fund treasury management Service Level Agreement.

A. Main issues arising

The Pension Fund maintains relatively small balances of cash arising from the receipt of employer and employee contributions exceeding payments made on behalf of the Fund. Most of the Fund's cash is managed externally, either by the investment managers or the Bank of New York Mellon, the Fund's custodian. The cash held by the administering authority is usually less than 1.0%, or £10m, of the Fund's assets providing a working balance for the Fund to meet its short term commitments. From time to time, if surplus cash balances held are greater than £10m and are greater than the amounts required for , then they are invested with the Fund's fund managers in accordance with the Investment Strategy.

Historically the Council has pooled Pension Fund cash with its own cash and paid interest to the Pension Fund at the Interbank Sterling LIBID 7 day rate. From time to time when the Pension Fund's cash balances have been higher than average; for example, prior to the implementation of a fund manager transition, funds have been invested with counterparties directly on behalf of the Fund in accordance with the Council's treasury management strategy. A call account solely for the use of Pension Fund cash was set up in summer 2009 to establish greater separation with only small balances pooled with the Council's cash to minimise the administration of the process.

Recently there has been national interest in the co-mingling of Council and Pension Fund investments and the Audit Commission raised this as an issue for further discussion during the 2008/09 Fund audit.

Usually an administering authority must not borrow money on behalf of the Pension Fund. Regulation 5 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 gives an administering authority the power to temporarily borrow on behalf of the Fund in order to pay benefits due or to meet investment commitments arising from a change in Investment Strategy. The temporary loan and interest should be repaid within 90 days of the date of the borrowing.

It is proposed that to facilitate greater transparency going forward all surplus Pension Fund cash should be managed in accordance with an SLA agreed by the Pension Fund Committee, thereby formalising the arrangements for investing the daily cash balances. Members are therefore asked to review and approve the SLA attached as Appendix 1. This SLA reflects processes already in place for the Fund. A copy of the Council's Treasury Management Strategy is attached as Appendix 2. The Treasury Management Strategy is due to be scrutinised by the Council's Regulatory and Audit Committee on 1 February.

C. Resource Implications

None.

D. Legal Implications

None.

E. Other implications / issues

During 2010, the Treasury Team will be working with the Fund's Actuary to develop more detailed cashflow analysis for the short and longer term alongside the triennial valuation activity.

F. Feedback from consultation and Local Member Views

Not applicable.

G. Communication Issues

None.

H. Progress Monitoring

Not applicable.

I. Background Papers

Pension Fund Committee 19 November 2009, agenda item 4.

Your questions and views

If you have any questions about the matters contained in this paper please get in touch with the Contact Officer whose telephone number is given at the head of the paper.

PROVISION OF TREASURY MANAGEMENT SERVICES By BUCKINGHAMSHIRE COUNTY COUNCIL TO THE BUCKINGHAMSHIRE COUNTY COUNCIL PENSION FUND

This is an agreement between the Pension Fund Committee and the Administering Authority Buckinghamshire County Council, such that:

1 A separate bank account operates for the purpose of the Pension Fund.

2 Based on the projected daily balances for the Pension Fund bank account, the BCC Treasury Team will process inter-company loans between the County Fund and the Pension Fund bank account so that the balance in the Pension Fund bank account is within +/-£5,000.

3 The Pension Fund's projected daily balances will be pooled with the Council's daily balances up to a maximum of £250,000. The Council will pay the Fund interest on the pooled balances at the Interbank Sterling LIBID 7 Day Rate (as published in the Financial Times), within 5 working days of the end of the month. The interest will be paid into the Pension Fund bank Account.

4 The BCC Treasury Team will invest the Pension Fund's remaining cash balances with counterparties on behalf of the Pension Fund in accordance with the County Council's treasury management strategy. Investments will usually be in an instant access call account since the Fund's money is primarily held to meet immediate payments from the Fund. Interest will be paid direct into the Funds Bank account at the agreed rate.

5 For any surplus balances estimated to be significant in cash terms and likely to remain for a significant period of time, the BCC Treasury Team will make every effort to place these surplus funds with Fund Managers in accordance with the Fund's Investment Strategy.

6 The BCC Treasury Team may arrange a temporary loan from a bank for up to 90 days in order pay benefits due under the Pension Fund Scheme or to meet investment commitments.

7 The BCC Treasury Team will check balances on the Pension Fund / Council cash adjustment codes every Friday and on the last working day of the month. Any balances on the cash adjustment account will be transferred to / from the Pension Fund.

This agreement is effective from 1 April 2010 and will be subject to annual review by the Pension Fund Committee.

BUCKINGHAMSHIRE COUNTY COUNCIL

TREASURY MANAGEMENT STRATEGY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2009/10

Treasury Management Strategy Statement

Introduction

1 The Treasury Management Strategy details the expected activities of the treasury function in the forthcoming year 2009/10. The publication of the strategy is a statutory requirement. This strategy incorporates the indicators required by the Prudential Code for Capital Finance which are elsewhere on the agenda.

2 The Treasury Management Strategy Statement and Annual Investment Strategy are underpinned by Treasury Management Practices which provide prescriptive information as to how the treasury management function should be carried out. The publication of a treasury management strategy statement is in line with the CIPFA Code of Practice.

Current Portfolio Position

3 The Council's treasury portfolio position as at 31 January 2009 comprised:

Borrowing			
Fixed Rate Funding:	**£234.6m**	**Average Rate:**	**6.3%**
Investing			
In House Investments:			
Call accounts	**£11.9m**	**Average Rate:**	**1.8%**
Money market loans	**£153.4m**	**Average Rate:**	**5.3%**

Prospects for Interest Rates

4 The Council has appointed Sector Treasury Services as a treasury adviser to the Council and part of their service is to assist the Council to formulate a view on interest rates. Sector's current interest rate view is that the Bank of England Bank Rate, the official Bank rate paid on commercial bank reserves, is:

- currently at 1.0%, because of the intensifying global recession, it is forecast to fall to 0.5% in Q4 2008/09
- Bank Rate is then expected to remain there until starting to rise gently up from Q1 2010/11 till it reaches 4.0% in Q4 2011/12
- there is a potential risk to these forecasts; if the recession proves to be deeper and more prolonged than currently expected then interest rates may not increase to the timescales forecast.

Borrowing Strategy

5 The Council's borrowing objectives are:

- to minimise the revenue costs of debt whilst maintaining a balanced loan portfolio
- to manage the Council's debt maturity profile, leaving no one future year with a disproportionate level of repayments

- to maintain a view on current and possible future interest rate movements and borrow accordingly
- to monitor and review the balance between fixed and variable rate loans against the background of interest rate levels and the Prudential Indicators.

Investments Strategy

6 This Council maintains investments that are placed with reference to cash flow requirements. Investment of the Council's funds will be in accordance with the Treasury Management Practices.

Debt Rescheduling

7 The potential for debt rescheduling is monitored in light of interest rate movements. Any rescheduling will be in accordance with the borrowing strategy. The reasons for rescheduling include:

- the generation of cash savings at minimum risk
- fulfilment of the borrowing strategy
- enhancement of the maturity profile of the borrowing portfolio.

8 All rescheduling will be reported retrospectively as part of the annual Treasury Management Activity Report.

Minimum Revenue Provision Policy Statement

9 In previous years the Council in accordance with legislation has made a contribution from revenue to cover 4% of the unfinanced borrowing that has been undertaken to support the capital programme. This contribution is called the Minimum Revenue Provision (MRP).

10 The Secretary of State under section 21(1A) of the Local Government Act 2003 issued new guidance on the calculation of MRP in February 2008. 2008/9 is the first year of operation.

11 Where capital expenditure was incurred before 1 April 2008 MRP will continue to be charged at the rate of 4% of the outstanding Capital Financing Requirement, in accordance with the guidance. For capital expenditure incurred on or after 1 April 2008 and funded through borrowing, the Council will calculate MRP using a more complex calculation called the asset life annuity method. Using this method MRP is calculated in a similar way as calculating the capital repayment element of a fixed rate repayment mortgage.

12 In accordance with provisions in the guidance, MRP will be first charged in the year following the date that an asset becomes operational.

13 Certain expenditure reflected within the debt liability at 31st March 2008 will under delegated powers be subject to MRP using the asset life annuity method, which will be charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure.

14 The asset life annuity method calculation requires estimated useful lives of assets to be input in to the calculations. These life periods will be determined under delegated powers to the Head of Finance, with regard to the statutory guidance.

15 However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the asset life annuity method would not be appropriate.

16 As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

Annual Investment Strategy

Introduction

17 This Council has regard to the Guidance on Local Government Investments issued in 2004 and CIPFA's Treasury Management in Public Services: Code of Practice and Cross Sectoral Guidance Notes.

18 The Annual Investment Strategy states which investments, specified and non-specified, the Council may use for the prudent management of its treasury balances during the financial year. These are listed in Schedule A.

19 This strategy sets out this Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

Investment Objectives

20 The general policy objective for this Council is the prudent investment of its treasury balances. The Council's investment priorities are the security of capital and liquidity of its investments. The Council will aim to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity. Investment of the Council's funds will be in accordance with the Treasury Management Strategy and Policy. All investments will be in sterling.

21 The Council's investments and strategy are reviewed on a monthly basis with the Cabinet Member for Resources. Additional reviews may take place during the year as necessary e.g. to respond to market conditions.

22 The Council's treasury management ensures it has sufficient cash to meet its needs, balancing achieving value for money with the security of its investments (i.e achieving a balance between liquidity, security, and yield). Performance is monitored against its treasury management strategy and outcomes matched against benchmarks set out in the strategy. The Council meets any tax and prompt payment legislation (Late Payment of Commercial Debts (Interest) Act 1998).

23 The Department for Communities and Local Government (DCLG) maintains that the borrowing of monies purely to invest or lend on and make a return is unlawful and this Council will not engage in such activity.

Specified Investments

24 Specified investments seek to offer high security and high liquidity. These investments can be used with minimal procedural formalities. All these investments should be in sterling and with a maturity of no more than a year.

Non-Specified Investments

25 Investments in excess of 12 months or with bodies which do not have a high credit rating, e.g. UK nationalised banks which offer government backed open market rates, although the institutions do not have individual credit ratings in their own right and building societies which offer more attractive rates for taking smaller investment sums compared to other institutions in the money market, are known as non-specified. For non-specified investments proper procedures must be in place for undertaking risk assessments prior to investments being placed. Investment instruments identified for use in the financial year are listed in Schedule A under the specified and non-specified investments categories.

Security of Capital: The use of Credit Ratings

26 This Council relies on credit ratings published by Fitch Ratings to establish the credit quality of counterparties and investment schemes. The Council has also determined the appropriate credit ratings it deems to be "high" for each category of investment, and these are set out at Schedule B. Credit rated institutions are selected using criteria based on the country, also known as sovereign rating if the institution is not UK, support rating, long-term and short-term ratings and the institutions individual rating.

Monitoring of credit ratings:

- The Council has access to Fitch credit ratings and is alerted to changes through its use of the Sector website
- the Council invests in UK or specified AAA sovereign rated countries, the total maximum that can be invested in foreign institutions is £50m
- if a counterparty or investment scheme's rating is downgraded with the result that it no longer meets the Council's minimum criteria, the further use of that counterparty/investment scheme as a new investment will be withdrawn immediately
- if a counterparty is placed on negative rating watch indicating that a downgrade is either likely or possible in the future, then it will be removed immediately from the lending list
- if a counterparty is upgraded so that it fulfils the Council's criteria, its inclusion will be considered and put to the Head of Finance for approval.

Use of Specified and Non-Specified Investments

27 The use of specified and non-specified investments is limited to those set out in Schedule A. The Head of Finance will keep the use of such investments under continuous review in the light of risk, liquidity and return. No additions will be made without the approval of the Council.

Investment balances / Liquidity of investments

28 Based on its cash flow forecasts, the Council anticipates its fund balances in 2009/10 to range between £120m and £200m. A prime consideration in the investment of fund balances is liquidity and the Council's forecast cash flow. Investments are made in

accordance with this Annual Investment Strategy and the investment strategies approved by the Head of Finance during the year.

Provisions for Credit-related losses

29 If any of the Council's investments appeared at risk of loss due to default the Council will make revenue provision of an appropriate amount. This authority currently has a £5m investment locked in the Icelandic bank Landsbanki Islands. The Icelandic Government has stated its intention to honour all its commitments as a result of their banks being placed into receivership, and is working with the UK Government to help achieve this. At the current time it is not possible to say with certainty that the Council will recover the entirety of its investment or when reimbursements will be made to this Council. The UK Government informed local authorities in November 2008 that it intends to make a regulation to require local authorities to delay recognising any loss on these investments that may eventually be incurred until the financial year 2010/11.

End of year Investment Report

30 At the end of the financial year, the Cabinet Member for Resources will receive a report on investment activity as part of the treasury management activity report.

Background Papers

CIPFA Code of Practice on Treasury Management in the Public Service 2006
ODPM Guidance on Local Government Investments issued in 2004
Communities and Local Government Guidance on Minimum Revenue Provision issued February 2008.

Head of Finance
11 February 2009