

Pension Fund Committee

4 March 2015



Investment of the Pension Fund's cash balances

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Purpose of Report

1. To update the Committee of the Treasury Management service provided to the Pension Fund and to review the charges for the services and the calculation of interest on short term investments administered by the County Council for 2015/16.

Background

2. The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009 (the 2009 Regulations) introduced changes which ended the use of Pension Fund money by the administering authority.
3. As a result of the 2009 Regulations, a report was presented to the Pension Fund Committee in June 2010. At this meeting, the Pension Fund Committee gave its agreement to Durham County Council continuing to invest the cash balances of the Pension Fund in line with the County Council's Treasury Management Policy and Annual Investment Strategy. This agreement is reviewed annually and the County Council continues to invest the balances of the Pension Fund.
4. The County Council's Treasury Management Policy and Annual Investment Strategy sets out the maximum amounts and time limits in respect of deposits which can be placed with each financial institution.
5. The Pension Fund's cash balances are invested along with the County Council's cash balances at the most advantageous rate that can be achieved using approved counterparties.
6. Reports on the return on short term investments are presented quarterly to the Pension Fund Committee.

Administration of the Treasury Management Function

7. The Council's Treasury Management team administer the cash balances of the Pension Fund in line with the County Council's procedures.

8. The prime objective of the Council's investment strategy is to ensure prudent investment of surplus funds. The Council's investment priorities are therefore the security of capital, liquidity of investments and, within those objectives, to secure optimum performance.
9. The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration.
10. After this main principle the Council will ensure:
 - (a) It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security.
 - (b) It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.
 - (c) It maintains a counterparty list in compliance with the CIPFA Treasury Management Code of Practice and credit rating information supplied by the County Council's Treasury Management advisers and will revise the criteria and submit them to the Council for approval as necessary.
11. The Treasury Management team review and monitor the Council's Treasury Management Strategy on behalf of the Council and implement it on behalf of the Pension Fund. The team also update counterparties in line with information supplied by the Council's Treasury Management Advisers.
12. The Council's treasury management team monitors the cash, the bank account balances and the cash codes for the Council and the Pension Fund and actions the necessary transfers and coding adjustments. The Pension Fund balance is corrected for any incorrect banking of funds prior to calculation of the interest on the cash balance.
13. All bank charges incurred by the Pension Fund are recharged to the Pension Fund by the Treasury Management team,
14. The Treasury Management Team maintains full and accurate records in the performance of this service and makes them available for inspection by the Pension Fund Accounting Team, Internal and External Audit.
15. It is recommended that the fee for this service continue at the level set with effect from 1 April 2014, which is a flat fee of £2,500 per quarter

Calculation of Interest on Cash Balances

16. The interest paid to the Pension Fund in respect of its cash balances is based on the London Interbank Bid rate (LIBID) three month rate and it is recommended that this rate continues to be applied in 2015/16 .
17. The LIBID three month rate is the rate at which banks are willing to borrow from other banks, and is the closest to the return that the County Council make on their own short term investments.
18. However, the choice of the rate would be subject to review by the Treasury Management team, to ensure an appropriate rate is applied.

Investments

19. It was also agreed by the Committee, that the Pension Fund's cash balances would be invested as part of the County Council's overall investments.
20. As a result of this however, in the event of an investment being lost, for example due to the failure of a financial institution in which the cash is invested, the Council would be liable for the loss. This is due to the investment being in the name of the Council although the investment would include Pension Fund balances.
21. It was therefore agreed that the Pension Fund Committee share the risk of any investment in proportion to the value of cash balances at the time of investment. Any losses incurred as a result of impairment would then be split proportionately between the Council and the Pension Fund.
22. It is recommended that this arrangement continues.

Banking Arrangements

23. On 5 November 2013, the Council's current bank supplier (Co-operative Bank) advised it was withdrawing from the Local Authority market. The Council had previously negotiated a contractual extension until 31 March 2016 and the Co-operative Bank has committed to honour this extension.
24. The Council has since undertaken a procurement process and has formally awarded its banking contract to Lloyds Bank.
25. The contract is for an initial core period of five years, with the option to extend annually thereafter, based on positive performance and review.
26. The Pension Fund bank account is part of the Council's banking contract and is therefore included in the change of banking supplier to Lloyds Bank.
27. Work is now focussing on managing the transition from the Co-operative Bank to Lloyds Bank. This transition process is being carefully planned and it is expected that all functionality will have transferred to Lloyds by October 2015.

28. During this transition and going forward with Lloyds Bank, there may be changes to the processes in the treasury management function, which may necessitate additional time and cost being allocated to the Pension Fund.
29. This will be closely monitored throughout 2015/16 and, if necessary, further reports will be prepared to inform Members of changes impacting on the service being delivered.

Recommendation

30. It is recommended that, with effect from 1 April 2015:
 - (a) The Pension Fund continues to invest its cash balances with the Council in line with the Council's Treasury Management Strategy;
 - (b) Interest be paid quarterly to the Pension Fund at a rate based on the daily cash balance and the 3 month LIBID interest rate;
 - (c) An administration fee of £2,500 per quarter be paid to the Council for the Treasury Management function being carried out on behalf of the Pension Fund; and
 - (d) In the event of the loss of an investment, the Pension Fund will bear the loss in proportion of the value of cash balances held at the time of the investment with Durham County Council.

Background Papers

- (a) Pension Fund Committee – 21 June 2010 – The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009.
- (b) Pension Fund Committee – 7 March 2013 – Investment of the Pension Fund's Cash Balances
- (c) Pension Fund Committee – 6 March 2014 – Investment of the Pension Fund's Cash Balances
- (d) Durham County Council's Treasury Management Policy.

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