

The background of the slide features a large, light blue watermark of the City of Vancouver's coat of arms. The crest includes a crown with four maple leaves, a shield divided into four quadrants (top-left: a saltire, top-right: a stag's head, bottom-left: a sailing ship, bottom-right: an eagle), and a banner at the bottom with the motto 'A NE FOR A'.

## **Agenda Item 8**

# **Cash Management Policy**

**Falkirk Council**

**Subject: Cash Management Policy**

**Meeting: Joint Meeting of Pensions Committee and Pension Board**

**Date: 19 March 2020**

**Submitted by: Director of Corporate and Housing Services**

**1. Purpose of Report**

- 1.1 This report brings an updated version of the Cash Management Policy to the Committee and Board for approval.
- 1.2 The policy sets out the framework within which the Fund seeks to manage its cash holdings, so that balances are secure, accessible and sufficient to allow the Fund to meet its various obligations.

**2. Recommendations**

- 2.1 **The Committee and Board are asked to note the updated version of the Cash Management Policy.**
- 2.2 **The Committee is asked to approve the updated version of the Cash Management Policy**

**3. Background**

- 3.1 The Fund requires readily available cash to meet its daily operational needs, taking into account that at any given time, it may be receiving cash in the form of contributions from scheme members and employers, whilst simultaneously needing cash to make pension and lump sum payments.
- 3.2 Separately, the Management and Investment of Funds Regulations stipulate that any monies not immediately needed to pay for benefits should be invested.
- 3.3 The cash balances held by the Fund fall into two categories - "Operational Cash" and "Investment Cash".
- 3.4 "Operational Cash" is cash that is needed to meet day to day activities, such as the payment of scheme benefits and capital calls, whereas "Investment Cash" is cash that has arisen as a consequence of the Fund's investment strategy, such as distributions from private equity or infrastructure holdings.

- 3.5 The Cash Management Policy is intended to cover the arrangements for managing Operational Cash whereas Investment Cash is dealt with under the Fund's Investment Strategy.
- 3.6 In all circumstances, pension fund cash – whether operational or invested – is held separately and distinctly from the funds of Falkirk Council. In formulating the cash management policy, the Fund will however utilise the specialist expertise of the Council's Treasury team and the professional advice given to the Council as part of its own Treasury Management Strategy.
- 3.7 The Fund's Cash Management Policy has been updated to reflect the change in the Fund's banking arrangements from the Clydesdale Bank to the Royal Bank of Scotland; an extension to the range of approved counterparties; an increase in the maximum sums that may be deposited with each counterparty; and a section on anti-money laundering.

#### **4. Key Objectives and Controls**

- 4.1 The objectives of the Cash Management Policy are to ensure that cash holdings are held securely and with sufficient short term accessibility for the Fund to meet its ongoing obligations. The return to be achieved on the cash holdings is a secondary consideration.
- 4.2 The policy document sets out the arrangements and controls in place to meet the policy objectives. These include:
- the types of risk associated with cash management
  - the types of cash instrument in which the Fund may invest
  - the standard of creditworthiness required from a counterparty
  - the cash limits that may be deposited with counterparties, and
  - the maximum aggregate amount of Operational Cash that may be held
- 4.3 Under the terms of the policy, the Fund will only invest with counterparties which have a short term credit rating of at least F1 (i.e. the highest available) from the Fitch credit rating agency and which have also been approved by Falkirk Council as part of the Council's own Treasury management arrangements.
- 4.4. The maximum aggregate amount of Operational Cash to be held is set at £25m. It is possible that a combination of factors may require this limit to be breached in which case, this will be brought to the attention of the Chief Finance Officer and reported to the Committee and Board.

#### **5. Implications**

##### **Financial**

- 5.1 Cash management is a key part of the Fund's operations requiring there to be sufficient monies available to meet short term obligations and allowing surplus cash to be allocated for investment. The security and liquidity of cash in these circumstances is the immediate priority.

## **Resources**

- 5.2 There are no additional administrative resources associated with the report recommendation.

## **Legal**

- 5.3 There is a statutory requirement for the Fund to invest cash not immediately required for the payment of benefits and other obligations.

## **Risk**

- 5.4 Failure to properly manage its cash arrangements could result in the Fund having insufficient funds to meet its immediate obligations. The Cash Management Policy provides provide the framework for officers to undertake effective management of these assets.

## **Equalities**

- 5.5 There are no equality issues arising from this report.

## **Sustainability/Environmental Impact**

- 5.6 There are no sustainability/environmental issues arising from this report.

## **6. Conclusion**

- 6.1 The Cash Management Policy has been updated to reflect the current cash management arrangements.
- 6.2 Levels of cash are monitored regularly by officers and by the Joint Investment Strategy Panel.

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Date: 9 March 2020

## **Appendices**

Appendix 1 – Cash Management Policy

## **List of Background Papers:**

None



**Falkirk Council**

**FALKIRK COUNCIL  
PENSION FUND**

**CASH MANAGEMENT POLICY**

**February 2020**

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# 1. Introduction

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## **Overview**

The payment of pensions and other benefits to Scheme members requires that Falkirk Council Pension Fund (the Fund) has sufficient liquidity to meet its various obligations. This necessitates the careful management of the Fund's cashflow requirements.

This document sets out the guidelines through which cash operations are carried out by the Pensions Section.

The policy is framed within the terms of Falkirk Council's own Treasury Management Practices which have been developed by Council officers and treasury management advisers.

## **Nature of Cash Holdings**

The cash deposits held by the Fund can be separated into the categories of "Operational Cash" and "Investment Cash" as follows:

- Operational Cash is cash that is held to meet daily business obligations, such as the payment of scheme benefits and meeting capital calls; and
- Investment Cash is cash that has arisen as a consequence of the Fund's investment strategy, such as private equity distributions.

### *Operational Cash*

Operational Cash itself consists of two elements:

- Cash used for the payment of scheme benefits (e.g. pensions and lump sums) - this cash is deposited with the Royal Bank of Scotland who are the Fund's banker and with a small number of other counterparties.
- Cash used for the purpose of meeting capital calls, drawdowns - this cash is held with Northern Trust, the Fund's Custodian and banker for the purpose of processing investment instructions.

### *Investment Cash*

Cash as an investable asset is recognised as a distinct component within the Fund's strategic asset allocation. However, the strategic allocation to cash is 0% meaning that where an investment cash balance exists, the expectation is that it will be reduced, subject to factors such as prevailing economic circumstances and other more suitable investment opportunities being available. In recent years, given the low yield, high cost characteristics of the bond market, the Fund has held higher than normal cash balances as an alternative to buying bonds.

## **Cash Management Objective**

The main objective of the policy is to ensure that the Fund has sufficient cash in order to meet its day to day investment and scheme benefit obligations. Where cash is being held, the general rule is that it 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.

For the avoidance of doubt, it should 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.

## **2. Compliance**

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### **Local Government Pension Scheme**

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.

An authorised deposit-taker means:

1. a person who has permission under Part 4 of the 2000 Act (permission to carry on regulated activities) to accept deposits;
2. an EEA firm of the kind mentioned in paragraph 5(b) of Schedule 3 to the 2000 Act (EEA passport rights) which has permission under paragraph 15 of that Schedule (as a result of qualifying for authorisation under paragraph 12 of that Schedule) to accept deposits;
3. the Bank of England or the central bank of an EEA state other than the United Kingdom;  
or
4. the National Savings Bank.

(n.b. the "2000 Act" is the Financial Services and Markets Act 2000)

### **CIPFA Code of Treasury Management**

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. Cash Management activities are therefore carried out in accordance with the relevant Local Government Pension Scheme (LGPS) regulations and Codes of Practice as set out by CIPFA.



### 3. Risk Management

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The Chief Finance Officer is responsible for the design, implementation and monitoring of all arrangements for the control of cash management risk within the Fund. This involves reviewing from time to time 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 objective.

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 (deposit cash).

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 (investment); and
- the maximum length of deposit.

#### **2. Liquidity risk management**

Due to the level of highly liquid assets it holds, the Fund does not anticipate being in a situation where it would 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 this 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 cashflow positive situation it does not intend to engage in borrowing. It will instead use 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 retaining some flexibility should there be a change in the level of interest rates either generally or between counterparties.

### **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. Further information regarding currency risk can be found on Page 9.

### **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 (incl. money laundering)**

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 is made between those charged with setting cash management policies (i.e. the Pensions Committee) and those who will implement and control the policies (i.e. the Chief Finance Officer and Pensions Section Officers). Segregation of duties also exists at an operational level. Persons responsible for initiating transactions are separate from those authorising the transactions.

In relation to money laundering, any regulatory developments will be accessed, in the main, via the Council's treasury team, professional publications and the internet.

The Chief Finance Officer in conjunction with treasury management advisers has formulated suitable criteria, including credit rating and sector for assessing and monitoring the risk of investment counterparties. Investment activity will only be conducted with the institutions listed in Appendix A on the basis that they continue to be authorised to carry out relevant business in the UK.

The Chief Finance Officer acts as the Council's Money Laundering Reporting Officer and the Council has a Fraud section which the Fund has access to. Staff have been briefed by a Corporate Fraud officer on the need to report any suspicious transactions that could potentially be linked to money laundering or the proceeds of crime.

The Council also has a Whistleblowing and Anti-Fraud and Corruption Strategy which deals with the unauthorised use of public funds, fraud and corruption (including bribery) and any deliberate concealment of information relating to any of these issues.

## **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.

## 4. Investment & Counterparty Choice

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### Determining the Counterparty

In determining the type of “cash” deposit/investment to be made and who is an appropriate counterparty, the Fund will only use counterparties approved by 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 Council and the Fund have access to market data, including negative rating watches and other publicly available information in order to support monitoring of the 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.

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

\*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 the Fitch credit ratings agency (or equivalent) 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 Council's own banker (RBS) will continue to be used for all purposes while part nationalised. If RBS cease to be part nationalised and the bank is below the necessary criteria it will only be used for immediate banking needs and cash balances will be minimised where possible and maintained in an instantly accessible call account.

The minimum level of acceptable credit rating for an approved counterparty is as undernoted. As the Fund's aim is not to hold cash indefinitely, officers will pay particular attention to the short term rating whilst also having regard to the long term rating.

	Fitch	
SHORT TERM	F1	This rating indicates the strongest capacity for timely payment of financial commitments within a 12 month timeframe.
LONG TERM	A	This denotes high credit quality; a low expectation of credit risk; and 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'.

## 5. Operations

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Cash Flow management is the key element of the Fund's cash operations. Daily, weekly and quarterly cash flow monitoring and forecasting takes place with actual and projected balances being reviewed by Fund officers and collaborative partners - Lothian Pension Fund Investments (LPFI).

The Fund's main cash inflows and outflows are as follows:

Source	Cash Element
Pensioner Payroll	Payments made to pensioners on the 15th of each month
Pension Contributions	Receipts from employers due by the 19 <sup>th</sup> of the month after contributions have been deducted from pay (22 <sup>nd</sup> if paid electronically)
Creditor Payments	Monies are transferred from the Fund to the Council to cover creditors payments on behalf of the Fund (e.g. retirement lump sums) . The amounts will vary from week to week.
Misc. Payments and Receipts	Irregular during the month and depends on demand, such as transfers in or out of the Fund
Investments	Drawdowns 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 counterparties where credit ratings fail to match stated criteria;
- Reviewing lending limits and maturity periods of individual counterparties;
- Authorising pension fund transactions in line with Council's approved arrangements; and
- Approving the Fund's list of authorised signatories.

### Role of Authorised Signatories (other than Chief Finance Officer)

- Authorising pension fund transactions in line with Council's approved arrangements.

### 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:

- Managing cash flow and Fund banking arrangements;
- Managing risk associated with the Fund's immediate liabilities and surplus funds;
- Making deposits in accordance with approved counterparty list;
- Diversifying cash across range of approved counterparties so as to reduce risk; and
- Assessing and recommending for approval new financial instruments and cash management techniques

## **Cash Limits**

Where cash is held to allow 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 Appendix A. These include the limits placed on the Fund's bank and custodian as noted below.

Royal Bank of Scotland - £8 million

Northern Trust - £10 million (n.b. investment cash may also be held with Northern Trust)

The above should be interpreted as maximum limits rather than investment targets. Aggregate cash for operational purposes from all accounts should not exceed £25 million.

### **Royal Bank of Scotland**

The Royal Bank of Scotland operates the Fund's current and business reserve accounts with automatic sweeping arrangements in operation between both accounts. The reserve account earns a base interest rate of 0.3% (as at March, 2020).

The Fund does not have an overdraft arrangement with the Royal Bank of Scotland. However, the relationship that the Council has with the bank allows an overdraft facility to be made available when required at favourable terms.

The Royal Bank of Scotland will continue to be used for transactional purposes even if the bank falls below the Fund's required credit rating criteria. However, if this occurs, balances will be minimised and generally maintained in the current account where there is instant accessibility.

### **Northern Trust**

Northern Trust are the Fund's appointed custodian. 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 earmarked for further investment by managers and b) cash held centrally for deployment in the Fund's alternatives programme. Only the cash held centrally is deemed to be under internal management and covered by this policy document.

All monies that are held centrally are automatically swept into one of Northern Trust's AAA rated money market funds, allowing balances to earn additional interest at minimal risk. Where the level of (investment) cash held by Northern Trust on behalf of external Fund Managers is deemed excessive, this will be considered by the Joint Investment Strategy Panel and potentially raised with managers.

## **Currency**

The Fund's cash management activities do not involve investment in foreign currency instruments. The exception to this is the funding and receipt of alternative investments where transactions are in foreign currency. These are done via Northern Trust with foreign currency balances being converted to sterling at the end of each month or converted to the Northern Trust Euro Cash Fund. This helps avoid exposure to negative Euro interest rates which would otherwise apply. Euro Funds are kept to the minimum and are used only to meet capital call obligations payable in Euros. This also reduces the need and the costs associated of having to purchase/sell currency to meet commitments.

## **Ancillary Systems**

Officers use the undernoted IT systems to support the Cash Management Operations:

- Logotech – A database providing cash flow management and interest rate forecasting.
- Royal Bank of Scotland Bankline System – This is a web based application providing real time detail of account positions; CHAPS and Faster Payments facilities; and inter account transfers.

# **6. Policy Review**

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The Policy will be reviewed on an annual basis and any material changes reported to the Pensions Committee and Board.

Chief Finance Officer  
March 2020



# Appendix A

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## Pension Fund - List of Approved Counterparties

Counterparty	Maximum Limit of Investment £m	Maximum Length of Deposit
<b>Banks</b>		
Royal Bank of Scotland*	£8m	Call
Barclays Bank	£8m	95 days
HSBC	£8m	95 days
Lloyds Banking Group#	£8m	95 days
Santander UK	£8m	95 days
Standard Chartered	£8m	95 days
Sumitomo Mitsui Banking Corporation Europe	£8m	95 days
<b>Building Societies</b>		
Nationwide	£5m	95 days
Coventry	£5m	95 days
<b>Money Market Funds</b>		
AAA rated funds Northern Trust (as Fund Custodian)	£8m £10m	Call
<b>UK Government</b>	Unlimited	95 days

\* Includes National Westminster Bank.

# Includes Bank of Scotland.

At time of writing (March 2020), the Fund has deposits with the Royal Bank of Scotland, the Bank of Scotland, Santander UK and Northern Trust.