National Pensions Reserve Fund
Commission

National Pensions Reserve Fund Commission
Report and Financial Statements
for the period 2 April 2001 to 31 December 2001

Contents

Treasury Building,
Grand Canal Street, Dublin 2, Ireland.
Telephone: (353 1) 664 0800
Fax: (353 1) 664 0890

National Pensions Reserve Fund
Commission

28 June 2002

Mr. Charlie McCreevy, T.D.,
Minister for Finance,
Government Buildings,
Upper Merrion Street,
Dublin 2

Dear Minister,

I have the honour to submit to you the Report and Accounts of the National Pensions Reserve Fund for the period from 2 April 2001 to 31 December 2001.

Yours sincerely,

Donal J. Geaney
Chairman

Chairman's Statement

This is the first annual report of the National Pensions Reserve Fund Commission. The Commission and the Fund were established under the National Pensions Reserve Fund Act, 2000 and came into operation on 2 April 2001. On its inception a total of €6,515 million (both capital and interest) was transferred to the Fund from the Temporary Holding Fund for Superannuation Liabilities. Allowing for €972 million in GNP related Exchequer contributions in 2001 and for interest earned and certain administration expenses in the year, the Fund amounted to €7,715 million at 31 December 2001.

The purpose of the Fund is to partially prefund the cost of social welfare pensions and public service pensions. It is not an overstatement that every member of the Irish population has a stake in the Fund and I am conscious of the responsibility placed on myself and my fellow Commission members with respect to the prudent management of the Fund's resources.

The first few months of the Fund's existence have been dynamic. With the help of advice from external consultants and from the National Treasury Management Agency, the Commission decided on the Fund's long-term strategic investment benchmark including its risk diversification parameters. The Commission also decided on the appropriate investment manager structure for the Fund and its market entry strategy. Global tenders were held for the appointment of institutional investment managers, a global custodian and a transition manager. In the case of the investment managers almost 600 applications were received for a total of 15 separate mandates. These applications have now been processed and the managers appointed. A global custodian has been appointed for the safekeeping of assets. A transition manager has also been appointed in order to ensure the Fund's smooth and efficient entry to the international capital markets. Performance and risk reporting systems requirements have been specified and installed. New investment categories are under consideration.

Over the last few months the Fund has gradually moved from cash to being substantially invested. The fact that so much has been achieved within a relatively short time period owes much to the effort and commitment of my fellow commissioners and the staff in the NTMA involved in the planning and execution of its investment strategy and I would like to record my deep appreciation of their effort.

Donal J. Geaney
Chairman

28 June 2002

Standing Left to Right: Mr. Robert J. Curran, Mr. Daniel P. Tully, Dr. Michael J. Somers, Mr. Donald C. Roth
Seated Left to Right: Dr. Martin Kohlhaussen, Ms. Brid Horan, Mr. Donal J. Geaney

National Pensions Reserve Fund Commission

Legislative Background

The National Pensions Reserve Fund Act, 2000 provides for

- the establishment of the National Pensions Reserve Fund to meet as much as possible of the cost to the Exchequer of social welfare and public service pensions from 2025 to at least 2055;
- the payment into the Fund of moneys in the Temporary Holding Fund for Superannuation Liabilities and the winding-up of that Fund;
- the payment each year from 2001 to at least 2055 from the Central Fund of a sum equivalent to 1% of GNP, supplemented by such additional payments as may be approved by Dáil Éireann;
- the establishment of the National Pensions Reserve Fund Commission (a body corporate consisting of 7 commissioners) with absolute discretion to control, manage and invest the assets of the Fund, acting through the Manager;
- the appointment by the Commission for a period of 10 years of the National Treasury Management Agency as Manager of the Fund;
- the delegation by the Commission to the Manager of any of its functions as it considers appropriate or expedient;
- moneys in the Fund to be held or invested by the Commission in or outside the State so as to secure the optimal total financial return, as to both capital and income, provided the level of risk to the moneys held or invested is acceptable to the Commission and that the moneys are not invested in Irish Government securities;
- the appointment by the Commission of investment managers, custodians, consultants and other service providers;
- the assessment by the Commission, from time to time, of the projected profile of Exchequer outlays on social welfare and public service pensions;
- commencing in 2025, and continuing until not earlier than 2055, the making of payments by the Commission from the Fund to the Exchequer on the request of the Minister for Finance in accordance with rules to be approved by resolution of the Dáil;
- the charging to the Central Fund of the expenses of the NTMA in performing its function as Manager;
- the charging to the National Pensions Reserve Fund of all other expenses;
- the audit by the Comptroller and Auditor General of the accounts of the Fund;
- the publication by the Commission of an annual report of its activities and of the audited accounts of the Fund.

The chairperson of the Commission is required to appear before and give evidence to the Committee of Public Accounts of Dáil Éireann on the policies of the Commission in relation to the Fund. The chief executive officer of the Manager is required to give evidence to the Committee on the regularity and propriety of all transactions on the Fund and on the economy and efficiency of the Commission and the Manager in regard to the expenses of operation of the Fund.

Donal J. Geaney **Chairman**

Senior advisor to Elan Corporation plc, Chairman of Irish Aviation Authority and director of a number of companies.

Mr. Robert J. Curran

Former Second Secretary in the Department of Finance.

Ms. Brid Horan

General Manager Pensions, ESB.

Dr. Martin Kohlhaussen

Chairman of the Supervisory Board, Commerzbank AG, Frankfurt.

Mr. Donald C. Roth

Managing Partner, Emerging Markets Partnership, Washington DC and former treasurer of the World Bank.

Dr. Michael J. Somers

Chief Executive of the National Treasury Management Agency (ex-officio member).

Mr. Daniel P. Tully

Chairman Emeritus of Merrill Lynch & Co. Inc., Connecticut.

Establishment of Commission and Fund

By order under section 3 of the National Pensions Reserve Fund Act, 2000 the Minister for Finance appointed 2 April 2001 as the establishment day; on that day the National Pensions Reserve Fund Commission and the National Pensions Reserve Fund came into existence.

The following persons were appointed members of the Commission by the Minister for Finance on the establishment day:

Mr. Donal J. Geaney (Chairman)

Mr. Robert J. Curran

Ms. Brid Horan

Dr. Martin Kohlhaussen

Mr. Donald C. Roth

Dr. Michael J. Somers

Mr. Daniel P. Tully

The Chairman is appointed for 5 years, Dr. Martin Kohlhaussen, Mr. Donald Roth and Mr. Robert Curran for 4 years, Mr. Daniel Tully and Ms. Brid Horan for 3 years. The ex-officio member holds office for such period as he or she is chief executive officer of the National Treasury Management Agency. The Commission met formally on 6 occasions during the period April to December 2001. These meetings included a two-day meeting in June 2001 to determine the Fund's long-term asset allocation and strategic benchmark. There were also a number of informal meetings, notably in the run-up to the June meeting.

At its inaugural meeting on the establishment day, the Commission appointed the NTMA as Manager of the Fund, in accordance with section 21(2) of the Act.

Payments into Fund

On 6 April 2001, the moneys in the Temporary Holding Fund for Superannuation Liabilities totalling €6,515 million were transferred into the Fund. Further sums totalling €972 million and representing the one per cent of GNP contribution were paid into the Fund in three quarterly instalments during 2001. Pending the appointment of investment managers the Fund was held entirely in cash, which was kept on deposit with a large number of banks both in Ireland and overseas. The Fund earned interest, net of expenses, of €228 million during the period to 31 December 2001, equivalent to an annualised return of 4.4%, and on that date totalled €7,715 million.

Reports to Minister for Finance

The Commission is obliged to submit an Annual Report to the Minister. This Report, while having regard to the need for open and transparent reporting on the operation of the Fund, but subject to preserving confidentiality in regard to commercially sensitive information, is to include information on the following:

- Investment strategy.
- Investment return.
- Valuation of the net assets.
- Investment management and custodianship arrangements.
- Fees, commission and other expenses incurred by the Commission and by the Manager.

INVESTMENT STRATEGY

The objective of the National Pensions Reserve Fund is to meet as much as possible, within prudent risk parameters agreed by the Commission, of the cost to the Exchequer of social welfare and public service pensions to be paid from the year 2025 until at least the year 2055. The Commission agreed that its investment policy for the Fund, as provided for in section 19 of the Act, should have as its objective the maximisation of the terminal wealth of the Fund over the time scale as laid down in the Act. This should be done through an investment strategy which has due regard to the purpose of the Fund as set out in section 18 of the Act and the payment requirements as set out in section 20 of the Act. The Commission further agreed that a periodic assessment of the Fund's value, relative to the value of the liabilities for social welfare pensions and public service pensions during the period from 2025 to 2055, should be carried out to determine the funded status of such pensions as represented by the accumulated value of the Fund. In the interim, and particularly at the end of each accounting year, the progress of the Fund will be measured against benchmarks decided by the Commission in the context of the investment strategy of the Fund.

The Commission determined that, in deciding on the Fund's long-term investment strategy, the main asset classes open to the Fund would be bonds (other than Irish Government securities – the Fund cannot, under section 6 of the Act, invest in them) and equities. It requested the NTMA to hold a competition for the selection of an advisor on strategic long-term asset allocation and portfolio construction. Following this competition, and on the recommendation of the NTMA, the Commission agreed to appoint Mercer Limited as advisor.

Mercer used Modern Portfolio Theory to produce an 'efficient frontier' for the portfolio. Efficient frontier analysis involves the construction of a set of alternative diversified portfolios each of which has the minimum expected risk for a given expected return. The 'efficient frontier' plots the expected return against risk for all portfolios which have been optimised with respect to risk/return combinations. This technique relies fundamentally on the continuation, within specified limits, of past correlations between different assets and asset classes. It is a useful tool for decision making but cannot, of course, foretell the future.

The recommendations from Mercer, following detailed discussions with the NTMA and as presented to the Commission, were that, given the long-term nature of the Fund's liabilities, the broad asset allocation at the commencement of the Fund's operations should be 80% equities and 20% bonds. In that regard a critical and necessary assumption was the equity risk premium i.e. the additional reward that a long-term investor in equities can reasonably expect as compensation for the fact that equity returns are inherently more volatile than bond or cash returns. The long-term equity risk premium was assumed to be 3% per annum. The Mercer recommendations were adopted by the Commission.

Benchmark Portfolio Structure

Having made the long-term strategic asset allocation decision, the Commission then considered the more detailed structure of a benchmark portfolio against which the Fund would be managed in the medium to long-term and which would also determine the investment mandates to be awarded to investment managers. The Commission approved the following combination of assets proposed by Mercer, on the basis of efficient frontier analysis, as the benchmark for the Fund:

Asset Class	% Allocation	Regional Splits	% Allocation
Eurozone Equities	40%		
Non-Eurozone Equities	40%	US	26.4%
(50% hedged)		Europe ex Eurozone	6.8%
		Japan	5.2%
		Pacific Basin	1.6%
Total Equities	**80%**		
Eurozone Bonds	**20%**		

The above table sets out the initial allocation of assets, with the weights for each region in the non-Eurozone area based on the mid-2001 market capitalisation in the FTSE All-World Developed Index, adjusted to reflect long-term strategic regional preferences. These regional weightings will be subject to variation on a quarterly basis as the market capitalisations change. There are a number of other smaller asset classes that may be appropriate given the Fund's characteristics and long -term investment horizon. These include small capitalisation quoted equities, property, emerging markets, private equity and corporate bonds. The Commission has initiated a study on whether these other classes would appear on the efficient frontier and, if so, whether and how they might be incorporated in a developed benchmark.

Also, as indicated above, the Commission decided, based on Mercer's advice, to adopt a currency overlay strategy which would hedge half of the non-Eurozone foreign exchange exposure.

INVESTMENT RETURN

The Commission considered whether for the period up to end-2001, when the external investment managers were expected to be appointed, arrangement should be made for the Fund to gain interim market exposure. It was agreed that financial futures represented the only viable means through which such exposure could be gained.

However, if over the period to end-year equity markets fell, any exposure through the financial futures would result in the Fund incurring realised losses. In the circumstances and given the particular uncertainties attaching to short-term market prospects, the Commission decided against adopting an interim strategy.

The assets of the Fund were accordingly held in cash from 6 April 2001 to 31 December 2001, pending the selection of investment managers. The Commission delegated to the NTMA authority to manage the cash against a short-term benchmark of an equal mix of 1, 3 and 6 months deposits at Euribor minus 5 basis points, provided at least 75% of the investments matured before December 2001 and 100% matured before March 2002. In the period under review the Fund earned an interest return of 3.27% compared to the short-term benchmark return of 3.24%; by way of contrast the long-term benchmark would have generated a negative return (minus 3.5%) over the same period. The Fund has, since year-end, moved to a substantially invested position, in line with its chosen investment policy.

VALUATION OF FUND'S ASSETS

Valuation of the National Pensions Reserve Fund for the period 2 April 2001 to 31 December 2001

	€	€
Transfer from Temporary Holding Fund for Superannuation Liabilities		
Capital contributions by Minister for Finance	6,156,959,942	
Interest received and accrued on deposits	357,921,234	6,514,881,176
Paid in by the Minister for Finance –1 per cent of GNP for 2001		971,984,499
		7,486,865,675
Interest received and accrued on deposits 2 Apr. to 31 Dec. 2001		228,677,358
Sub-total		7,715,543,033
Transfer to Administration Account (expenses)		(951,598)
Balance in Fund on 31 December 2001		7,714,591,435

As the Fund was held in cash over the entire period there were no capital gains or losses.

INVESTMENT MANAGEMENT AND GLOBAL CUSTODY ARRANGEMENTS

Investment Manager Structure/Risk Budgeting

The Commission, having decided on the asset allocation, then determined the manager structure. In the first instance consideration was given to whether there should be balanced managers, each dealing with multiple asset classes, or specialist managers each dealing with a particular asset class. The Commission accepted Mercer's advice that there is a strong case for employing specialist managers.

In accordance with conventional practice the Commission next considered the degree of additional risk (i.e. additional to that inherent in the strategic benchmark which research suggests typically accounts for around 90% of a fund's risk and return) which it was prepared to accept from employing a mix of active and passive managers. Active managers can only be justified if there is a reasonable expectation that they can add value over and above any extra costs incurred. This involves an element of risk in pursuit of a higher return. In that regard the risk measure used most frequently, and the one adopted by the Commission, is the concept of tracking error. Tracking error is a statistical measure of the volatility of an actual return versus a benchmark return; it measures the standard deviation of the differences between the return on the actual and the benchmark portfolios. Simply put, a tracking error of 2% implies that two-thirds of the time an active manager's return can be expected to be within ± 2% of their benchmark. Having taken into account advice from Mercers, as well as the policies adopted by and experience of other similar funds internationally, the Commission decided that it was reasonable to take on limited active manager risk, with an overall tracking error target for the Fund as a whole in the range 1% to 1.5% relative to the long-term strategic benchmark, on an annualised basis.

On the basis of the above, the Commission decided on the following investment management mandates (each equity portfolio to be measured against its constituent in the FTSE All World Developed Index and the bonds to be measured against the Merrill Lynch Eurozone Bond Index, excluding Ireland) and their associated tracking error targets:

Asset Class	Investment Style	% Allocation	Tracking Error Targets
Eurozone Equity (2 managers)	Passive[1]	27.9	0.10%
Pan-European Equity (3 managers)	Active[2] - Core	13.0	5.00%
US Equity	Passive	9.0	0.10%
US Equity	Enhanced	5.2	1.50%
US Equity	Active - Value	4.4	6.00%
US Equity	Active - Growth	4.4	6.00%
Japanese Equity (2 managers)	Active	4.4	6.00%
Pacific Basin Equity	Active	1.3	6.00%
Global Equity (2 managers)[3]	Active - Core	10.4	6.00%
Euro Bonds	Passive	14.8	0.25%
Euro Bonds	Active	5.2	2.00%

[1] *Under passive investment (sometimes also called indexation) the manager's job is to reproduce, with a minimum degree of variation, the return recorded by a specific market index or another benchmark.*

[2] *Active management involves the manager making stock selection decisions and at times asset allocation decisions with a view to out-performing a specific market index.*

[3] *The benchmark for Global Equity is a composite of 50% FTSE Eurobloc and 50% FTSE All-World Developed ex-Eurobloc.*

The above disposition of the Fund is approximately 50% active and 50% passive as follows:

	% Passive	% Active
Bonds	14.8	5.2
Equities	36.9	43.1
Total	51.7	48.3

The Commission decided that at this stage around 16 was the optimal number of investment managers to be appointed to the Fund, having regard to the trade-off between the marginal benefit of improved diversification and the higher fee costs associated with a greater number of managers. Adding more managers decreases overall risk, but the benefits from diversification diminish in size as more managers are added. The Commission further decided to delegate to the NTMA responsibility for the passive bond management and the currency overlay.

The Commission directed the NTMA to conduct a competition under EU public procurement rules for the selection of institutional investment managers for the other mandates. Following a competitive tender in which eleven consultancy firms were invited to submit detailed proposals, the Commission accepted the NTMA's recommendation that the Frank Russell Company be appointed as consultants to advise on the manager selection process.

In accordance with advice from legal counsel, the investment manager selection process was conducted under the restricted procedure provided for under Public Service Directive 92/50/EEC. In sum, as stipulated in the Directive, the process was carried out in two stages as follows:

Stage One: Publication of a Notice in the Official Journal of the EU inviting Investment Managers to submit expressions of interest in tendering.

The Notice was published on 5 July 2001 and, after the mandatory minimum 37 days allowed for the preparation of responses, 581 expressions of interest from some 200 managers were received. In anticipation of a large volume of interest, the NTMA created a special electronic tendering website on which investment managers were invited to register their expressions of interest by responding to a detailed questionnaire prepared by the NTMA in consultation with the Frank Russell Company.

Stage Two: 178 invitations to tender sent to some 100 Investment Managers selected under Stage One.

The tender documents stipulated that the contracts would be awarded to the most economically advantageous tenders and in that regard the criteria to be applied would be as follows:

- Strength of the firm.
- Resources.
- Calibre of the individuals involved.
- Relevant experience.
- Quality of risk control framework.
- Quality of administration and reporting.
- Ability to manage conflicts of interest.
- Fee.
- Historical performance.
- Ability to meet investment objectives.
- Terms of legal agreement/contract to which the investment manager would be subject.

Allowing for the mandatory minimum period for preparation of tenders, the deadline for receipt of replies was 22 October 2001. 158 valid tenders were received from 88 managers. Following a rigorous evaluation process the appointment of 15 managers was ratified by the Commission as follows:

Eurozone Equity Passive portfolios:
- Barclays Global Investors .... **€1.1 billion**
- Bank of Ireland Asset Management/ State Street Global Advisors..................... **€1.1 billion**

US Equity Passive portfolio:
- Barclays Global Investors .... **€690 million**

Pan European Equity Active Core portfolios:
- Putnam Investment Limited .... **€335 million**
- Blackrock International .... **€335 million**
- Bank of Ireland Asset Management Limited .... **€335 million**

US Equity Enhanced Index portfolio:
- Invesco Asset Management Limited . **€420 million**

US Equity Active Growth portfolio:
- Goldman Sachs Asset Management International .... **€410 million**

US Equity Active Value portfolio:
- Lord, Abbett & Co .... **€340 million**

Japanese Equity Active portfolios:
- Daiwa SB Investments Limited .... **€125 million**
- J.P. Morgan Fleming Asset Management (UK) Ltd .... **€125 million**

Pacific Basin ex Japan Equity Active portfolio:
- Schroder Investment Management Ltd... **€93 million**

Global Equity Active portfolios:
- Dresdner RCM Global Investors .... **€420 million**
- Capital International .... **€420 million**

Eurozone Long Bond Active portfolio:
- Irish Life Investment Managers Limited .... **€420 million**

The total value of the above mandates (which allows for the quarterly instalment of the GNP-related contribution payable in March 2002) is approximately €6.7 billion. In addition, as stated above, the NTMA manages a passive euro bond portfolio, valued at approximately €1.2 billion. The value of the individual portfolios will vary depending on market conditions and manager performance and as ongoing cash flow may be directed to them from time to time.

Transition Manager

The function of a transition manager is to purchase, in an efficient and cost effective manner on behalf of the Fund, the securities required by the individual institutional investment managers. This arrangement enables the costs incurred in market entry to be quantified and controlled; for example, it achieves economies of scale by block purchases of stocks on behalf of the different managers. It seeks to minimise the costs of market impact through careful timing of the execution of trades. It also avoids unintended biases during a transition period; for example, if all investment managers were to purchase securities in one particular sector in advance of others, the portfolio would have an unintended bias during the transition. It also avoids any ambiguity with respect to a manager's accountability for investment performance during the market entry stage. Watson Wyatt were appointed, following a competitive tendering process, to advise on the selection of a transition manager. As in the case of the investment managers, in accordance with legal advice the selection process for transition manager was conducted under the restricted procedure of the relevant EU Public Procurement Directive. Under Stage One of the procedure, expressions of interest were received from 12 firms all of whom were invited to submit tenders under Stage Two: 12 tenders were received. The tender documentation provided that the contract be awarded on the basis of the most economically advantageous bid in accordance with the following criteria:

- Strength of the firm.
- Resources available for transition management.
- Calibre of the individuals involved.
- Relevant experience in transition management.
- Quality of risk control framework.
- Ability to minimise the cost of implementing the transition.
- Quality of administration and reporting.
- Ability to manage conflicts of interest.
- Fee.

Morgan Stanley & Co. International Limited was duly appointed as Transition Manager.

Global Custody

Essentially a custodian is responsible for the safekeeping of a fund's assets independently of the investment managers. A further competition under the restricted procedure of the EU Public Procurement Directive was held for the selection of a global custodian for the Fund. Following a competitive tendering process, Bacon and Woodrow were retained to advise on the selection. Expressions of interest in tendering for the position of global custodian were received from 12 firms, 11 of whom were invited to submit tenders: 10 tenders were received. Following evaluation of the tenders the Commission appointed ABN Amro Mellon as Global Custodian. The global custody services involved are:

- **Transaction Settlement:** This involves the delivery of cash or securities in respect of purchases/sales of the Fund's assets etc.
- **Safekeeping:** This service deals with the holding in safe custody of all securities and other assets in the ownership of the Fund and the issuance of confirmations that such assets are held to the order of the Fund. An essential part of this service is the maintenance of accurate records and the issuance of reports to the Fund and certificates to auditors confirming the details of assets in custody.
- **Collection of Income and Dividends on Assets:** This involves the monitoring and collection of dividend payments and interest payments on securities, the conversion of foreign currency receipts and the deployment of the cash as directed by the Fund manager.
- **Claiming Tax Refunds:** This function requires a detailed knowledge of the tax laws in each country as they relate to the particular securities held and, where appropriate, claiming refunds of tax deducted from interest, dividends and other income.
- **Cash Sweeps:** This involves nightly investment by the custodian at market rates of residual cash in the various sub-portfolios.
- **Fund Accounting and Reporting:** This service provides a comprehensive range of reports such as financial accounting statements and mark to market reports.
- **Securities Lending:** This facility provides the Fund with the opportunity to earn additional income through lending securities to acceptable counter-parties with minimal risk.

FEES, COMMISSIONS AND OTHER EXPENSES

Expenses of Commission

Under section 26(1) of the National Pensions Reserve Fund Act, 2000 the Commission is required to include in its Annual Report a separate account of the administration fees and expenses incurred by them in the operation of the Fund. These are detailed below:

2 April 2001 to 31 December 2001	€
Salaries & expenses of Commission	213,554
Fund Manager fees	Nil
Global Custodian fees	Nil
Legal fees	120,592
Consultancy fees	605,633
Other fees and expenses	11,819
Total	**951,598**

The above expenses conform with the operating budget adopted by the Commission under section 6 (1)(g) of the Act.

In addition to these expenses, the costs incurred by the National Treasury Management Agency in its role as Manager amounted to €1.94 million. In accordance with section 23 of the Act these costs were charged on the Central Fund.

GUIDELINES ON CONFLICTS OF INTEREST

For the purposes of the guidelines provided for in section 12(7) of the National Pensions Reserve Fund Act, the Commission has determined that each of the interests contained in the Second Schedule to the Ethics in Public Office Act, 1995 shall constitute an 'interest'. The Commission has also determined that, in line with section 17 of the Ethics in Public Office Act, 1995, there should be an annual disclosure statement (the 'Annual Statement') prepared by each member of the Commission, any member of a committee established by the Commission and any designated member of staff of the Manager. Such Annual Statements are filed with the Compliance Officer of the NTMA. The foregoing section 12 guidelines were published in Iris Oifigiúil on 18 January 2002.

NATIONAL PENSIONS RESERVE FUND

COMMISSION MEMBERS AND OTHER INFORMATION

COMMISSION MEMBERS

Mr. Donal J. Geaney (Chairman)

Mr. Robert J. Curran

Ms. Brid Horan

Dr. Martin Kohlhaussen

Mr. Donald C. Roth

Dr. Michael J. Somers

Mr. Daniel P. Tully

BANKERS

Central Bank of Ireland

AUDITORS

Comptroller & Auditor General

Treasury Building

Dublin Castle

Dublin 2

MANAGER

National Treasury Management Agency

Financial Statements of the National Pensions Reserve Fund for the period 2 April 2001 to 31 December 2001

INVESTMENT REPORT

The Commission determines the investment strategy for the Fund, which was invested at 31 December 2001 as follows:

	€'000	% of Total
Equities		
No assets held in this category	Nil	Nil
Bonds		
No assets held in this category	Nil	Nil
Deposits		
Austria	149,106	1.9%
Belgium	324,206	4.2%
Spain	5,096	0.1%
France	52,463	0.7%
Germany	872,014	11.4%
Ireland (Commercial Banks)	1,023,102	13.3%
Ireland (Central Bank of Ireland)	2,800,693	36.5%
Italy	242,915	3.2%
Luxembourg	249,084	3.2%
Netherlands	285,013	3.7%
Portugal	199,755	2.6%
Sweden	5,101	0.1%
United Kingdom	1,464,710	19.1%
	7,673,258	100%

Donal J. Geaney
Chairman of Commission

Michael J. Somers
Chief Executive
National Treasury Management Agency (as Manager)

26 June 2002

STATEMENT OF COMMISSION'S RESPONSIBILITIES

The Commission is required by the National Pensions Reserve Fund Act, 2000 to prepare financial statements in respect of its operations for each financial year.

In preparing those statements, the Commission is required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- Prepare the financial statements on the going concern basis unless it is inappropriate;
- Disclose and explain any material departure from applicable accounting standards.

The Commission is responsible for keeping in such form as may be approved by the Minister for Finance all proper and usual accounts of all moneys received or expended by it and for maintaining accounting records which disclose with reasonable accuracy at any time the financial position of the National Pensions Reserve Fund and the administrative costs of the Commission.

The Commission is also responsible for safeguarding assets under its control and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Donal J. Geaney
Chairman of Commission

Michael J. Somers
Chief Executive
National Treasury Management Agency (as Manager)

26 June 2002

REPORT OF THE COMPTROLLER AND AUDITOR GENERAL

Report of the Comptroller and Auditor General for presentation to the Houses of the Oireachtas

I have audited the financial statements on pages 32 to 39 in accordance with section 26 of the National Pensions Reserve Fund Act, 2000.

Respective Responsibilities of the Commission and of the Comptroller and Auditor General

The accounting responsibilities of the Commission are set out in the Statement of Commission's Responsibilities on page 30. It is my responsibility, based on my audit, to form an independent opinion on the financial statements presented to me by the Commission and to report on them.

Basis of Audit Opinion

In the exercise of my function as Comptroller and Auditor General, I conducted my audit of the financial statements in accordance with auditing standards issued by the Auditing Practices Board and by reference to the special considerations which attach to State bodies in relation to their management and operation.

An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Fund's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations that I considered necessary to provide me with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In my opinion, proper books of account have been kept by the Commission and the financial statements which are in agreement with them properly present the results of the Fund's operations for the period ended 31 December 2001 and its balances at that date.

John Purcell
Comptroller and Auditor General

28 June 2002

ACCOUNTING POLICIES

The National Pensions Reserve Fund was established under the National Pensions Reserve Fund Act, 2000. The significant accounting policies adopted in respect of the National Pensions Reserve Fund are as follows:

Basis of preparation

The financial statements have been prepared in accordance with the National Pensions Reserve Fund Act, 2000 in a format approved by the Minister for Finance. The financial statements are also prepared in accordance with the standards of the Statement of Recommended Practice of the Consultative Committee of Accountancy Bodies.

The financial statements summarise the transactions and net assets of the National Pensions Reserve Fund. They do not affect the Exchequer's liabilities to pay pensions and other benefits in the future.

Reporting Period

The reporting period is 2 April to 31 December 2001. The Commission has adopted the calendar year as its financial year.

Reporting Currency

The reporting currency is the euro, which is denoted by the symbol €.

Valuation of Investments

Investments are stated at mid-market value for quoted investments at the year-end for the individual asset categories, by geographical location and by investment manager in note 3 to the financial statements. Unquoted investments are stated at market value estimated by the NTMA, as Manager of the Fund, based on professional advice. Realised and unrealised capital gains and losses on investments are dealt with in the Fund account in the year in which they arise. As the Fund was held on deposit during the reporting period, this accounting policy did not arise in respect of that period.

Investment income

Income from investments is accounted for on an income receivable basis.

Expenses

Expenses are accounted for in the year in which they fall due.

Foreign Currencies

Receipts and payments in foreign currencies are translated into euro at the rates of exchange prevailing at the date of receipt. Assets and liabilities in foreign currencies are translated into euro at the rates of exchange ruling at the year-end dates. Currency gains or losses arising from transactions during the year and from the conversion of year-end investment balances are included as part of the movement in the accumulated Fund for the year. No exchange gains or losses arose during the reporting period as all deposits were in euro.

FUND ACCOUNT
for the period 2 April 2001 to 31 December 2001

	Notes	Period ended 31 December 2001 €
Contributions	1	7,486,865,675
Investment return for the period		
- Investment income	2	228,677,358
- Change in market value of investments	3	Nil
Gross payments into Fund		7,715,543,033
Transfer to Administration Account	4	(951,598)
Net payments into Fund		7,714,591,435
Increase in Fund during the period		7,714,591,435
Net Assets of Fund at 2 April 2001		Nil
Net Assets of Fund at 31 December 2001		7,714,591,435

There were no gains or losses on the Fund account in the reporting period.

Donal J. Geaney	Michael J. Somers
Chairman of Commission	Chief Executive
	National Treasury Management Agency (as Manager)

26 June 2002

The statement of accounting policies and notes 1 to 12 form part of these accounts.

NET ASSETS STATEMENT

31 December 2001

	Notes	2001 €
Investment Assets	3	7,673,257,623
Current Assets	6	
Accrued interest on deposits		41,704,898
Current Liabilities	7	
Accrued expenses		(371,086)
Net Assets of Fund at 31 December 2001		7,714,591,435

Donal J. Geaney
Chairman of Commission

Michael J. Somers
Chief Executive
National Treasury Management Agency (as Manager)

26 June 2002

The statement of accounting policies and notes 1 to 12 form part of these accounts.

ADMINISTRATION ACCOUNT

for the period 2 April 2001 to 31 December 2001

	Notes	Period ended 31 December 2001 €
Transfer from Fund Account	4	951,598
Expenses of Commission	5	(951,598)
Net income\(expenditure)		Nil

Donal J. Geaney
Chairman of Commission

Michael J. Somers
Chief Executive
National Treasury Management Agency (as Manager)

26 June 2002

The statement of accounting policies and notes 1 to 12 form part of these accounts.

NOTES TO THE ACCOUNTS

1. Contributions	Period ended 31 December 2001 €
Paid in by the Minister for Finance – 1 per cent of GNP	971,984,499
Transfer from Temporary Holding Fund for Superannuation Liabilities	6,514,881,176
	7,486,865,675

2. Investment Income	Period ended 31 December 2001 €
Income from investments (being interest earned on deposits)	228,677,358

Summary of Investment Income from	2001 €
- Equities	Nil
- Bonds	Nil
- Cash	Nil
- Deposits	228,677,358
	228,677,358

3. Investment Assets	2001 €
(a) Summary of Assets	
- Equities	Nil
- Bonds	Nil
- Cash	Nil
- Deposits	7,673,257,623
	7,673,257,623

There was no change in the market value of deposits.

NOTES TO THE ACCOUNTS (continued)

(b) Analysis by geographical classification of Assets	2001 €
Europe (all denominated in euro)	7,673,257,623
	7,673,257,623

(c) The movement in the market value of investments held by the Fund during the year was as follows:		2001 €
Market value as at 2 April 2001		Nil
Transfer to Fund (Note 1)		7,486,865,675
Purchases at cost	27,921,570,390	
Proceeds of sales	(27,734,597,930)	
Net cash movement		186,972,460
Expenses of Commission actually paid		(580,512)
Change in market value of investments		Nil
Market value at 31 December 2001		7,673,257,623

Net cash movement reconciled to Investment Income	2001 €
Interest received in cash	219,983,485
Accrued interest on transfer from Temporary Holding Fund	(33,011,025)
Net cash movement	186,972,460
Closing interest accrual	41,704,898
Investment income (Note 2)	228,677,358

Deposits are 100% of the net assets of the Fund at 31 December 2001.

(d) The following investment manager holds the assets of the Fund:	2001 €
National Treasury Management Agency	7,673,257,623
	7,673,257,623

4. Transfer to Administration Account

This amount of €951,598 represents the amount required to cover the administration costs of the Commission.

5. Expenses of Commission

Under section 26(1) of the National Pensions Reserve Fund Act, 2000, the Commission is required to include a separate account of the administration fees and expenses incurred by it in the operation of the Fund. These are detailed below on an accruals basis:

	Period ended 31 December 2001 €
Salaries & expenses of Commissioners	213,554
Fund Manager fees	Nil
Global Custodian fees	Nil
Legal fees	120,592
Consultancy fees	605,633
Other fees and expenses	11,819
	951,598

In addition to the above expenses, the costs incurred by the National Treasury Management Agency in its role as Manager amounted to €1.94m. These costs are charged on the Central Fund and are excluded from the above.

6. Current Assets

	2001 €
Accrued interest on deposits	41,704,898
	41,704,898

7. Current Liabilities

	2001 €
Accrued expenses	371,086
	371,086

8. Taxation

The income and profits of the National Pensions Reserve Fund are exempt from corporation tax in accordance with section 30 of the National Pensions Reserve Fund Act, 2000.

9. Commitments

The notional and market value of derivative contracts entered into on behalf of the National Pensions Reserve Fund at 31 December 2001 was nil.

10. Contingent Liabilities

In the opinion of the Commission the National Pensions Reserve Fund had no contingent liabilities at 31 December 2001.

11. Related Parties

(a) Minister for Finance

As set out in note 1, contributions to the National Pensions Reserve Fund are to be made by the Minister for Finance by an annual charge on the Central Fund equivalent to 1 per cent of Gross National Product (GNP) under section 18(2) of the Act. The Minister for Finance may make such additional payments to the National Pensions Reserve Fund as are approved by Dáil Éireann under section 18(5) of the Act.

The commissioners of the National Pensions Reserve Fund, as given on page 25, were appointed by the Minister for Finance under section 7 of the Act.

(b) National Treasury Management Agency

Under section 21 of the National Pensions Reserve Fund Act, 2000, the National Treasury Management Agency was appointed as Manager of the Fund by the Commission for 10 years.

12. Approval of Financial Statements

The financial statements were approved by the Commission on 25 April 2002.

NOTES