

TEESSIDE PENSION FUND COMMITTEE

A meeting of the Teesside Pension Fund Committee was held on 27 September 2017.

PRESENT: Councillors Bloundele, (Chair), Brady, Coupe, Dean, Lewis, McGloin and Rostron

Other Local Authority Members:
Beall, Stockton Borough Council
Massey, Redcar and Cleveland Borough Council

ALSO IN ATTENDANCE: Property Advisors: A Owen and A Peacock
Unison Representative: A Watson
EY, External Auditor Representatives: N Armstrong and S Kenny
Aon Hewitt: M Ferguson

OFFICERS: J Bromiley, P Campbell, G Hall, S Lightwing, R Walker, J Weston

APOLOGIES FOR ABSENCE were submitted on behalf of Councillors G Purvis, Sharrocks and Walters, and P Fleck.

DECLARATIONS OF INTERESTS

Name of Member	Type of Interest	Item/Nature of Interest
Councillor Brady	Non Pecuniary	Member of Teesside Pension Fund
Councillor Beall	Non Pecuniary	Member of Teesside Pension Fund
Councillor Rostron	Non Pecuniary	Member of Teesside Pension Fund

17/18 **MINUTES - TEESSIDE PENSION FUND AND INVESTMENT PANEL - 28 JUNE 2017**

The minutes of the meeting of the Teesside Pension Fund and Investment Panel held on 28 June 2017 were taken as read and approved as a correct record.

17/19 **DRAFT REPORT AND ACCOUNTS**

The 2016/2017 Draft Annual Report and Accounts for the Teesside Pension Fund were presented for information. The Annual Report and Accounts provided an opportunity for stakeholders to be updated on recent changes to the Fund's membership, income and expenditure and the change in the size of the Fund's investment assets.

The membership of the Fund had increased, with total membership at the year-end now standing at 68,829, an increase of 2,040 over last year. The number of active members had increased by 1,154 (5.1%) over the year, and increased by 0.5% over the past five years, reversing a trend of decreases in membership when measured on a five year basis. The numbers of pensioners increased by 478 (2.2%) over the year, and increased by 10.5% over the past five years. The number of deferred members increased last year by 408 (1.7%), and increased by 9.3% over the past five years.

The contributions received from active members increased during 2016/2017 by £831,000 from the previous year. However, lump sum and benefit payments grew again by almost £6 million compared to 2015/2016.

The biggest change was the increase in new assets from £3.13 billion to £3.86 billion, a rise of over £726 million in the year. The main contributor to this rise was the strong equity market rally over the year and the change to currency rates, with the Fund's overseas assets rising as a result of a weaker Pound.

Investment income continued to rise, this time by £7.84 million, as investments continued to be made in equities and property, and more dividend and rent income was received.

There had been a decrease in management expenses between 2015/2016 and 2016/2017. CIPFA guidance required transaction costs to be included in the investment management costs. For 2015/2016 transaction costs were approximately £2.1 million compared to only £1.3 million in 2016/2017. The transaction activity was much reduced through last year, particularly investment asset purchases with the markets rising.

The aim of the Fund was to be 100% funded, and at the latest valuation the actuary was able to declare a funding level of 100%. This allowed many of the employers in the Fund to decrease the amount of their contribution for the next three years, releasing money for front-line services. The next valuation was due to be carried out in March 2019.

The Council adopted International Finance Reporting (IFRS) from 1 April 2010 and the Pension Fund accounts complied with the reporting standards.

ORDERED that the Annual Report and Accounts 2016/2017 were adopted.

17/20

TEESSIDE PENSION FUND AUDIT RESULTS REPORT - YEAR ENDED 31 MARCH 2017

The External Auditor presented the Teesside Pension Fund Audit results report. Subject to satisfactory completion of one outstanding item, the Auditor expected to issue an unqualified opinion on the Fund's financial statements on 28 September 2017. The only item that was outstanding was receipt of the signed management representation letter, as expected.

The Auditor highlighted several key points from the report as follows:

The level of materiality had increased from £31.3m at the planning phase to £38.5m on receipt of the actual year-end figures. The threshold for reporting audit differences had remained at £1.5 million as agreed with the Panel on 28 June 2017.

The areas of audit focus included three significant risks:

- Valuation of complex pooled investment vehicles.
- Valuation of directly held properties.
- Management override.

The Auditor confirmed that no issues had been identified during testing.

The Auditor's opinion on the financial statements was detailed at Section 3 of the submitted report and was a clean opinion.

A summary of adjusted differences was provided at Section 4 of the submitted report and the Auditor confirmed that there were now no uncorrected misstatements. The information presented in the Accounts represented a true and fair view.

The Auditor drew the Panel's attention to issues in relation to the Contribution Monitoring Spreadsheet. There had been a few minor discrepancies which, although they did not have any impact on the audit opinion, could be improved in future.

The Auditor was pleased to report that the Fund had acted on previous recommendations in relation to governance arrangements and good progress had been made.

Cyber Security and the EU's General Data Protection Regulation (GDPR), (which would come into effect from 25 May 2018), were highlighted as developing risks that Panels across the country should consider. The Head of Investments and Treasury confirmed that the Fund already had plans in place to review GDPR and would take advice and consider the issue of cyber crime.

ORDERED that the Teesside Pension Fund Audit results report for the Year ended 31 March 2017 was received and noted.

17/21 **FUND MANAGER'S REPORT**

A report of the Strategic Director Finance, Governance and Support was presented to inform Members how the Investment Advisors' recommendations were being implemented and to provide information with regard to stock selection strategies, including a detailed report on transactions undertaken.

In terms of implementation of the investment advisors' advice for the period April-June 2017, the Fund had continued avoiding bonds given the current yield. The Fund had invested, or divested out of equities, where appropriate depending on market levels. The Fund had continued to make progress on Property and Alternatives.

A summary of the Equity Returns for the Fund in the quarter to 30 June 2017 was included at 4.2 of the submitted report and showed a positive return in all by the US equity market. A Transaction Report was attached at Appendix A and overall there were net sales of approximately £17 million in the period, compared to net sales of £35 million in the previous reporting period. Cash balances increased from £444 million to £484 million.

The Head of Investments and Treasury informed the Panel of an investment in Arconic Inc which was the company involved in supplying the cladding used in Grenfell Tower in London. The purchase of 7500 shares had been made ahead of the fire disaster and the share price had now fallen significantly. No further purchases had been made and there was a watching brief on the share price.

The Fund Valuation detailed all the investments of the Fund as at 30 June 2017, and was prepared by the Fund's custodian, BNP. The total value of all investments, including cash, was £3,889 million. This compared with the last reported valuation, as at 31st March 2017 of £3,859 million.

An analysis of the summary valuation showed the Fund's percentage weightings in the various asset classes, compared with the Fund's customised benchmark and the advisors short term asset allocation range.

ORDERED that the report was noted.

17/22 **INVESTMENT ADVISORS' REPORT**

A report was presented to update Members with the current capital market conditions, and set an appropriate short term asset allocation to best take advantage of the conditions.

Since there were currently no Independent Investment Advisors in place to provide advice, a report from the Head of Investments and Treasury Management setting out the political, economic and market background since the previous meeting was attached at Appendix A to the submitted report.

In light of there being no Advisors to provide advice, it was considered appropriate to continue with the previous short term asset allocation. The current political, economic and market conditions were similar to previous advice provided at meetings and did not suggest any need to make any major strategy changes.

ORDERED as follows that:

1. The report was noted.
2. There was no change to the short term asset allocation.

17/23 **CBRE PROPERTY REPORT**

The Fund's Property Advisors submitted a report that provided an overview of the current

property market and informed Members of the individual property transactions relating to the Fund.

At 30 June 2017 the portfolio comprised 24 mixed-use properties located throughout the UK with a value of £206.65m. This reflected an overall Net Initial Yield of 5.15% and an Equivalent Yield of 5.84%.

There were no sales or acquisitions during the Q2 period from 17 April to 9 August 2017.

The Portfolio was currently circa £225m and the Property Advisors were currently working on another acquisition which, if successful, would bring the Fund close to its £250m target.

The Fund had recently completed the purchase of the Royal Mail Distribution Warehouse in Team Valley, Gateshead. The Fund purchased the property at 5.22% NIY, 5.78% EY which equated to £16,150,000. Two rent reviews had been completed, both resulting in an uplift. A new tenant was being sought for a unit in Cirencester since the previous tenant had gone into Administration. A further three rent reviews had commenced where uplifts were anticipated and an update would be provided at the next meeting.

ORDERED that the report was noted.

17/24

GOVERNANCE REVIEW - UPDATE

A report of the Strategic Director Finance, Governance and Support was presented to inform Members of the Teesside Pension Fund and Investment Panel of progress to date with the governance review.

Since the last meeting, the outstanding policies and strategies had been completed and were attached to the submitted report for Members approval as follows:

- Governance Policy and Compliance Statement (Appendix A)
- Officers' Scheme of Delegation (Appendix B)
- Administration Strategy (Appendix C)
- Communication Strategy (Appendix D)

A report would be submitted to Council in November 2017 seeking approval for amendments to the terms of reference for both the Panel and Board.

ORDERED as follows that the following documents were approved :

1. Governance Policy and Compliance Statement (Appendix A)
2. Officers' Scheme of Delegation (Appendix B)
3. Administration Strategy (Appendix C)
4. Communication Strategy (Appendix D)

17/25

FUNDING UPDATE REPORT - 2017

A report of the Strategic Director Finance, Governance and Support was presented to inform Members of the Teesside Pension Fund and Investment Panel (the Panel) of the outcome of the Actuary's Funding Update Report, as at 31 March 2017.

There were no direct financial implications from the update report, however, it provided an indication as to how the performance of the Fund's assets had impacted on its funding level, and a guide to progress towards the next Actuarial Review, due in 2019.

A copy of AON Hewitt's report was attached at Appendix A to the submitted report. The report was based on the movement in the Fund's assets over the period since 31 March 2016, but did not consider changes to the Fund's membership base. A comparison to the 2016 Actuarial Valuation was detailed at 5.2 in the report and showed that the funding level was now 118% with a surplus of nearly £600m. The improved funding level was due to the large increase in

the Fund's assets (a return of 24.9% over 2016/2017). This put the Fund in a good position going into the next Actuarial Valuation and confirmed that the current investment strategy had worked well to date.

In terms of the future service rate, the Actuary calculated that in the current market conditions they would propose to increase the future service rate by 1%. This changed the discount rate at which the future liabilities were rated to 16.7% on average. However, given the size of the surplus of £600m, if that figure was used to discount the future service rate this would bring a contribution rate of 8.8% in the future if set in 2019. This was entirely down to the change in market value and the valuation of the Fund.

It was confirmed that this report is an update for information only and a change to employer contribution costs would not be effected until the next triennial evaluation was carried out in 2019. However, in light of the rise over 2016/2017, the Fund would be reviewing its asset strategy.

ORDERED that the report was received and noted.

17/26 **GMP RECONCILIATION REQUIREMENTS**

A report was presented to provide an overview of requirement to undertake a reconciliation of each member's Guaranteed Minimum Pension (GMP) held by the Teesside Pension Fund and that held by HMRC's National Insurance Contributions Office (NICO).

For the period from 6 April 1978 to 5 April 2016 the Local Government Pension Scheme (LGPS) was contracted out of the State Second Pension (S2P), previously known as State Earnings Related Pension Scheme (SERPS). Although pension schemes could be contracted out of S2P/SERPS until 5 April 2016, only the period to 5 April 1997 accrued a Guaranteed Minimum Pension (GMP). The GMP was therefore the minimum benefit that a scheme had to pay to account for the fact the member had not accrued S2P/SERPS benefits from the State and could result in a higher benefit being payable than normally paid by the LGPS.

The HMRC's scheme support service was being withdrawn from 31 December 2018 and responsibility for maintaining GMP records would be handed over to pension schemes. The cost of reconciling scheme data to that held by HMRC had the potential to be high.

The Teesside Pension Fund had a total of 36,152 members who had left the scheme by 6 April 2016 and required additional investigation under stage 2 of the reconciliation process put forward by Kier Business Services Ltd, which equated to an estimated cost of £252,200. In order to ensure that the Teesside Pension Fund was obtaining value for money, initial quotes had been obtained for outsourcing this process which were much higher than Kier's estimate. Details of the stages required to complete the reconciliation work were attached at Appendix A to the submitted report.

ORDERED as follows:

1. The report was received and noted.
2. The undertaking of the second stage of the reconciliation process was approved.

17/27 **TREASURY MANAGEMENT REPORT**

A report on the treasury management of the Fund's cash balances, including the methodology used, was presented.

The counterparty list and associated limits as at 30 June 2017 were detailed in the report. As at 30 June 2017, the Fund had £468.0m invested with approved counterparties at an average rate of 0.282%.

Attached at Appendix A to the submitted report was a graph showing the maturity profile of cash invested along with the average rate of interest received on the investments.

Ordinarily, the Treasury Manager was under instruction to keep at least 50% of cash

investments relatively liquid (one month or less), in order to fund pension payments and investments. However, given the size of the cash assets held, this strict level was relaxed while cash levels were this high to allow cash flows to be managed at more sensible levels.

At 30 June 2017, 47.1% (£220.5m) of the investments matured within one month.

ORDERED that the report was noted.

17/28 **EXCLUSION OF PRESS AND PUBLIC**

ORDERED that the press and public be excluded from the meeting for the following items on the grounds that, if present, there would be disclosure to them of exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972 and that the public interest in maintaining the exemption outweighed the public interest in disclosing the information.

17/29 **POOLING UPDATE**

A report was presented to update Members of the latest developments in setting up the new Pool: Border to Coast Pension Partnership (BCPP).

ORDERED as follows that:

1. The report was noted.
2. The Responsible Investment Policy and Schedule of Governance were approved.

17/30 **NEWRIVER REIT TRANSACTION**

A report was presented to inform Members of a recent transaction with Newriver Reit.

ORDERED that the report was noted.