

TEESSIDE PENSION FUND COMMITTEE

A meeting of the Teesside Pension Fund Committee was held on Wednesday 9 December 2020.

PRESENT: Councillors D Coupe (Chair), E Polano (Vice-Chair), J Beall, A Bell, B Cooper, S Dean, T Furness, J Hobson, G Nightingale, J Rostron, Z Uddin and T Watson

ALSO IN ATTENDANCE: W Bourne (Independent Adviser), P Moon (Independent Adviser), A Owen (CBRE), M Rutter (External Auditor) (Ernst Young) and A Stone (Border to Coast Pension Partnership)

OFFICERS: S Lightwing, W Brown, D Johnson, J McNally, N Orton and I Wright

APOLOGIES FOR ABSENCE: were submitted on behalf of P Fleck

20/26 **DECLARATIONS OF INTEREST**

Name of Member	Type of Interest	Item/Nature of Interest
Councillor Beall	Non pecuniary	Member of Teesside Pension Fund
Councillor Cooper	Non pecuniary	Member of Teesside Pension Fund
Councillor Rostron	Non pecuniary	Member of Teesside Pension Fund
Councillor Uddin	Non pecuniary	Member of Teesside Pension Fund

20/27 **MINUTES - TEESSIDE PENSION FUND COMMITTEE - 16 SEPTEMBER 2020**

The minutes of the meeting of the Teesside Pension Fund Committee held on 16 September 2020 were taken as read and approved as a correct record.

20/28 **INVESTMENT ACTIVITY REPORT**

A report of the Director of Finance was presented to inform Members of the Teesside Pension Fund Committee how the Investment Advisors' recommendations were being implemented.

A detailed report on the transactions undertaken to demonstrate the implementation of the Investment Advice recommendations and the Fund's valuation was included, as well as a report on the treasury management of the Fund's cash balances and the latest Forward Investment Programme.

The Fund continued to favour growth assets over protection assets and currently had no investments in Bonds.

The cash levels at the end of September 2020 were 10.9%, which was approximately £430 million, a reduction of £43 million. The Fund had made significant commitments to private markets investments and as money was drawn down, the cash balance would reduce further. The Fund would continue to use cash to move away from its overweight position in equities and invest further in Alternatives. The Fund had sold £50 million in US equities during the quarter. Following recent discussions with Advisors, proposals for reducing the Fund's overweight position in equities would be presented to the next Committee meeting.

Investment in direct property would continue on an opportunistic basis where the property had good covenant, yield and lease terms. No property transactions were undertaken in this quarter.

During the quarter, £83.5 million was invested in Alternatives. The Fund was considerably underweight its customised benchmark and, providing suitable investment opportunities were available, would look to increase its allocation to this asset class up to the customised benchmark level.

Appendix A to the submitted report detailed transactions for the period 1 July 2020 to 30

September 2020. There were net purchases of £33.2 million in the period, this compared to net purchases of £22.8 million in the previous reporting period.

As at 30 September 2020, the Fund had £429.8 million invested with approved counterparties. This was a decrease of £43.1 million over the last quarter. Appendix B to the submitted report showed the maturity profile of cash invested as well as the average rate of interest obtained on the investments for each time period.

The total value of all investments as at 30 September 2020, including cash, was £4,084 million, compared with the last reported valuation as at 30 June 2020, of £4,150 million.

A summary analysis of the valuation showed the Fund's percentage weightings in the various asset classes as at 30 September 2020 compared with the Fund's customised benchmark.

The Forward Investment Programme provided commentary on activity in the current quarter as well as looking ahead to the next three to five years. Details of the current commitments in equities, bonds and cash, property and alternatives were included in paragraph 8 of the submitted report.

It was reported that work was continuing with Custodian to improve the accuracy of the Custodian report as there was still a variance.

ORDERED that the report was received and noted.

20/29

AUDIT RESULTS REPORT

The Auditor presented the provisional Audit Results Report for the Teesside Pension Fund for 2019/2020. EY had substantially completed the audit of Teesside Pension Fund for the year ended 31 March 2020. Subject to concluding the outstanding matters listed in Appendix D of the submitted report, the auditor confirmed that EY expected to issue an unqualified audit opinion on the financial statements. Any further amendments would be notified to the Committee.

The auditor highlighted the following items in the report:

- Materiality Thresholds.

The Auditor had previously reported that the materiality threshold used in the audit was £37.4 million, with a performance materiality of £28 million and an error-reporting threshold of £1.9 million. The thresholds had not been revised.

- Audit Opinion.

The audit opinion would include additional narrative to highlight financial statement disclosures that the valuations of directly held property had been prepared on the basis of a 'material valuation uncertainty'. These matters did not constitute a qualification of the audit opinion.

- Misstatements due to fraud or error.

There were no significant findings to report.

- Valuation of Investments.

The Covid-19 pandemic had had a significant impact on markets and investments in the Pension Fund and resulted in a reduction in the value of the Fund relative to the prior year. Following discussions with Officers and Investment Managers, the Auditor was confident that the impact of Covid-19 on valuations had been accurately reflected.

- Audit Differences.

A number of misstatements within the information used to prepare the accounts had been identified and these were listed at page 15 of the submitted report. The auditor highlighted that information received from the Custodian was not up to date and in one case there was

duplication of an investment that had been split during the year and both the original and split investments were recognised. The cumulative effect was a material overstatement in the draft accounts which was slightly above materiality. The majority of this had now been adjusted for in the final statements and the valuation of the Fund's assets decreased as a result. With these adjustments that Auditor confirmed that the valuation of assets in the accounts was materially correct.

- Directly Held Property.

EY's property experts reassessed the valuations of eight of the Fund's assets and was comfortable that these were appropriate. The Auditor noted however that valuations were at the upper end of the range.

- Audit Differences.

The total value was adjusted for was £33.1 million and £6.9 million that was not adjusted for. This was a combination of a £13.9 million that was a cumulative balance built up over a number of years. This would remain unadjusted as it was immaterial this year and would be looked at during 2020/2021 with the expectation that it would be cleared from the accounts for next year's audit. The 6.9 million was a cumulative impact of smaller differences between the Fund's records and investment managers. The Auditor confirmed that the opinion would be signed off with these amounts unadjusted.

- Recommendation.

The auditor had provided a recommendation in relation to a review of the information provided by the Custodian.

In conclusion, the Auditor confirmed EY's independence and highlighted the outstanding matters for completion of the audit. The auditor acknowledged the support and assistance of Council Officers during a difficult year.

ORDERED that the Audit Results Report 2019/2020 for the Teesside Pension Fund was received and noted.

20/30

EXTERNAL MANAGERS' REPORTS

A report of the Director of Finance was presented to provide Members with quarterly investment reports in respect of funds invested externally with Border to Coast Pensions Partnership Limited (Border to Coast) and with State Street Global Advisers (State Street).

As at 30 September 2020 the Fund had investments in:

- the Border to Coast UK Listed Equity Fund, which had an active UK equity portfolio aiming to produce long term returns of at least 1% above the FTSE All Share index; and
- the Border to Coast Overseas Developed Markets Equity Fund, which had an active overseas equity portfolio aiming to produce total returns of at least 1% above the total return of the benchmark (40% S&P 500, 30% FTSE Developed Europe ex UK, 20% FTSE Developed Asia Pacific ex Japan, 10% FTSE Japan).

For both sub-funds the return target was an annual amount, expected to be delivered over rolling 3 year periods, before calculation of the management fee. The Head of Pensions Governance and Investments reported that Border to Coast was performing well and meeting its target. Similarly State Street, which had a passive global equity portfolio invested across four different region tracking indices appropriate to each region, was also meeting its target.

The report highlighted that State Street had recently made changes to their passive benchmarks. State Street had advised investors in a number of its passively-invested funds, including the four State Street equity funds the Fund invested in, that it had decided to exclude UN Global Compact violators and controversial weapons companies from those funds and the indices they tracked. As this decision was taken by State Street in November, the performance information presented in the submitted report had not yet been impacted by this

change.

State Street had produced a Q&A document (included at Appendix C to the submitted report), setting out more detail of the potential investment impact of the change to benchmarks. Overall approximately 37 out of 2000 companies in the Overseas State Street passive fund were excluded and they represented about 3.6% of the index by value. It was highlighted that the anticipated impact on the performance of these funds and the Fund's investments was not huge.

The approach State Street was taking to companies that they did not wish to invest in was to exclude these companies from the underlying benchmarks. As a passive investor, this was one of the few approaches available as passive investment typically requires holdings in all the main components of a particular stock market index.

Active equity investors, such as Border to Coast, were able to make decisions on which companies to hold or the weighting to apply to each company based on a wide range of factors, including responsible investment: Environmental, Social and Governance issues (ESG) and the likely impact of those issues on the financial performance of that company. The Senior Portfolio Manager from Border to Coast provided a summary of Border to Coast's approach, the essence of which was to take a forward-looking view and anticipate changes to corporate behaviour, policies and approach. Border to Coast was reliant on a number of different data inputs and tried to get a broad source of inputs, as well as taking account of more qualitative and wide ranging ESG inputs. Border to Coast also tried to influence corporate behaviour through engagement.

In response to a Members' question, the Head of Pensions Governance and Investment commented that discussion had recently taken place with Border to Coast in relation to whether tobacco exclusion was something that should be reconsidered collectively. Although at the current time the majority of the Funds in Border to Coast would probably not agree to a tobacco exclusion, there was nothing to prevent this proposal being given further consideration and it remained on the agenda.

In relation to feedback from companies that had been excluded, the Head of Pensions Governance and Investment explained that it would take some time for this to happen but the ultimate aim was for companies to change their behaviour. It was suggested by the Investment Advisor that engagement was a better route than exclusion as it delivered better outcomes.

The Head of Pensions Governance and Investment highlighted that the Fund did not normally invest in passive funds and the aim, as previously discussed by the Committee, was ultimately to move funds from State Street into Border to Coast.

ORDERED that the report was received and noted.

20/31

LGPS - NATIONAL KNOWLEDGE ASSESSMENT

A report of the Director of Finance was presented to provide Members with information relating to the Local Government Pension Scheme (LGPS) National Knowledge Assessment, which was facilitated by Hymans Robertson.

In January 2019 the LGPS Scheme Advisory Board (SAB) commissioned Hymans Robertson to assist in delivering a review of governance across the LGPS. This review was termed the Good Governance Project. The review recognised the Pension Regulator's push to increase governance and administration standards in pension schemes, including public service pension schemes, for which it had oversight responsibility.

The Good Governance review set out proposals in six main areas and made recommendations, details of which were contained in the submitted report and appendices.

The Head of Pensions Governance and Investment highlighted that whilst there was a statutory duty on Members of Local Pension Boards to maintain an appropriate level of knowledge and understanding to carry out their role effectively, this did not currently apply to Members of the Committee. However it was suggested that this statutory duty would be amended to include Members of the Committee in future.

At meeting of the Teesside Pension Board held on 2 November 2020, Board Members had agreed to take part in the assessment process.

It was proposed that Members of the Teesside Pension Fund Committee should also participate in the Local Government Pension Scheme (LGPS) National Knowledge Assessment, to help assess the Committee's collective relevant LGPS knowledge with a view to facilitating targeted training to meet any training needs identified.

The cost of participating in the National Knowledge Assessment was £5,000 plus VAT and assuming full participation by the Committee and Board this equated to around £240 per person. The training would be arranged as quickly as possible.

ORDERED that Members of the Teesside Pension Fund Committee and the Teesside Pension Board would participate in the Local Government Pension Scheme (LGPS) National Knowledge Assessment facilitated by consultants Hymans Robertson.

20/32

BORDER TO COAST RESPONSIBLE INVESTMENT POLICY AND CORPORATE GOVERNANCE AND VOTING GUIDELINES

A report of the Director of Finance was provided to advise the Committee of recent changes made by Border to Coast Pensions Partnership Limited (Border to Coast) to its Responsible Investment Policy and Corporate Governance and Voting Guidelines.

Copies of both policies, with the changes highlighted, were attached as appendices to the submitted report, which also provided a summary of the main changes.

The following pre-work would be undertaken ahead of the 2021 Policy Review process:

- The development of a standalone climate change policy.
- The measurement of transition risk and the implications of setting targets, including the potential to set a net zero carbon target.
- The role of private markets in managing transition risk.
- Implications of an exclusion policy if engagement was ineffective.

Border to Coast would also continue to develop their communication approach to enable Partner Funds and other important stakeholders to understand and oversee Border to Coast in carrying out their responsible investment remit.

ORDERED as follows that:

1. the revised Border to Coast Responsible Investment Policy and Corporate Governance and Voting Guidelines included as tracked changes versions in Appendices A and B to the submitted report, were noted and approved.
2. the proposed areas for future development detailed in section 7 of the submitted report were noted.

20/33

PRESENTATION FROM BORDER TO COAST HEAD OF CLIENT RELATIONS

The Head of Client Relations, Border to Coast, gave a presentation which covered the following issues:

- Border to Coast Update
- Market Background
- Equity Investments Update
 - UK Listed Equity Fund
 - Overseas Developed Markets Equity Fund
- Alternatives Investments Update
 - Private Equity
 - Infrastructure

A timetable of the funds launched to date and those scheduled for 2021, 2022, and beyond were included in the presentation. Ten funds were now up and running and the Emerging

Market Hybrid would be launched early in 2021.

As at 8 October 2020, 91 people were now employed by Border to Coast, including a 12 investment team hires.

The Head of Client Relations highlighted Border to Coast's approach to equity management and responsible investment.

Details of the Fund's current investments with Border to Coast were also included in the presentation and information in relation to performance of the funds was also provided.

In response to a query raised by the Chair with regard to the Fund's investment in Apple, it was clarified that the portfolio weighting and dividends were in line with the benchmarks.

ORDERED that the presentation was received and noted.

20/34

INVESTMENT ADVISORS' REPORTS

The Independent Investment Advisors had provided reports on current capital market conditions to inform decision-making on short-term and longer-term asset allocation, which were attached as Appendices A and B to the submitted report.

Both Advisors provided further commentary at the meeting.

The major issue for the Fund's Portfolio was the overweight position in the strategic allocation and discussions were ongoing as to how this could be addressed. The Fund needed to continue reducing its equity holdings and investing in alternatives.

ORDERED that the information provided was received and noted.

20/35

CBRE PROPERTY REPORT

A report was submitted that provided an overview of the current property market and informed Members of the individual property transactions relating to the Fund.

Transactions remained much lower than last year at around 20-30% less. In terms of supply and demand there was not much change from the last update. Popular sectors included industrial, distribution and supermarkets. Retail, offices, and regions generally outside the south east were not popular. Retail was approaching the bottom of its market in terms of yields and there was beginning to be some interest in certain better quality assets in that sector. The alternative sector was relatively neutral, with care homes and the health side, as well as automotives, continuing to attract interest. Less popular sectors were pubs, leisure, and hotels. In line with previous years, people tended not to offer new properties to the market in December, as it was unlikely to transact and complete before the year end. It was expected that the market would return in the second half of January 2021.

In relation to the submitted report, the following issues were highlighted:

The acquisition of a highly regarded long-let supermarket detailed at page 6 of the report was no longer going ahead as the vendor had withdrawn from the sale.

As at 4 December 2020 the total Collectable Arrears on the portfolio had reduced to £935,000 as follows:

- River Island - arrears had increased to £233,000 and lease re-gear had been negotiated which would deal with the arrears.
- P and O Ferrymasters - the arrears had been cleared and a lease re-gear was being negotiated.
- Nuffield Health - negotiations were ongoing with regard to arrears and some rent had been paid.
- Peacocks Stores had entered into a CVA and the arrears had risen from £90,000 to £100,000, which would continue to rise. Until the Government's current protection scheme had ended it would not be possible to take possession of the property.

- Rugby were paying monthly and were on track with the payment plan.
- Boots were in negotiations to clear the current arrears.
- Sports Direct - arrears had risen to £94,000.
- Pizza Hut - a lease re-gear had been negotiated which would deal with the arrears.
- Marks and Spencer - the rent was being paid monthly but not the service charge and this issue was being resolved.
- Aurum Group Limited - rent was being paid monthly.

CBRE had collected 85% of the collectable rent to 10 November 2020, which was good in comparison to other Funds.

ORDERED that the information provided was received and noted.

20/36

XPS PENSIONS ADMINISTRATION REPORT

A report was presented to provide an overview of administration services provided to the Teesside Pension Fund by XPS Administration.

Updates were provided on the following items:

- Headlines - McCloud judgement.
- Regulations and guidance - the LGPS (Amendment) (No2) Regulations 2020- exit credits.
- Covid-19 - XPS update.
- Membership Movement.
- Member Self Service - new website.
- Additional Work - Guaranteed Minimum Pension reconciliation exercise.
- Complaints.
- Internal Dispute Resolution Process.
- Pensions Ombudsman.
- High Court Ruling.
- Annual Benefit Statements.
- Common Data.
- Conditional Data.
- Customer Service.
- Recruitment.
- Employer Liaison.
- Performance Charts.

ORDERED that the information provided was received and noted.

20/37

ANY OTHER URGENT ITEMS WHICH IN THE OPINION OF THE CHAIR, MAY BE CONSIDERED