TEESSIDE PENSION FUND COMMITTEE

A meeting of the Teesside Pension Fund Committee was held on 22 July 2020.

PRESENT: Councillors Coupe, (Chair), Bell, Cooper, Dean, J Hobson, J Rostron and Wright (As Substitute)

B Foulger, GMB Representative
A Watson, Unison Representative

Other Local Authority Members:
Councillor Beall, Stockton on Tees Council
Councillor Nightingale, Redcar and Cleveland Council

PRESENT BY INVITATION: Councillor C Hobson

ALSO IN ATTENDANCE: M Rutter, E Ferdani, EY

OFFICERS: S Bonner, W Brown, D Johnson, S Lightwing, C Lunn, N Orton

APOLOGIES FOR ABSENCE were submitted on behalf of Councillors Furness, Uddin and P Fleck.

DECLARATIONS OF INTERESTS

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
B Foulger	Non pecuniary	Member of Teesside Pension Fund

20/12 **MINUTES - TEESSIDE PENSION FUND COMMITTEE - 17 JUNE 2020**

The minutes of the meeting of the Teesside Pension Fund Committee held on 17 June 2020 were taken as read and approved as a correct record.

20/13 **DRAFT ANNUAL PENSION FUND REPORT AND ACCOUNTS 2019/20**

A report was of the Chief Finance Officer was presented to provide Members with the 2019/20 draft Annual Report and Accounts for the Teesside Pension Fund.

Although the report was in draft form there were unlikely to be any significant changes and the format and figures were correct.

The Head of Pensions Governance and Investment drew attention to the performance summary in the report and highlighted that there had been significant volatility in the markets in 2019/2020.

An initial increase in the Fund at the start of the year had been eclipsed by a large drop in global financial markets towards the end of the year as a consequence of the Covid-19 pandemic and concerns about the financial impact. That event had dominated the year and the financial outcome for the Pension Fund. Domestic issues which had previously seemed very significant; such as the 2019 General Election or the UK leaving the European Union on 31 January 2020, had been overshadowed by the impact of the pandemic. Similarly global issues such as US/China trade negotiations, as well as the nature of the eventual trading relationship between the UK and the EU, were also put to one side as the focus quickly moved to the impact of the pandemic on economies, industries, trade and growth. The Pension Fund was particularly affected because it was currently overweight in equities which had seen a dramatic and sudden fall towards the end of the year.

The financial performance for the Fund for the year was therefore negative. The Fund's value fell to approximately £3.74 billion - a decrease over the year of approximately £350 million. This drop in the Fund's value overshadowed the very positive outcome of the latest actuarial valuation of the Fund, the details of which were included in the submitted report. As at 31 March 2019 the funding level of the scheme had improved from 100% at the previous valuation, to 115%. This was third report in a row where the scheme had been declared fully funded.

The actuarial valuation report was published on 31 March 2020 and the Actuary considered whether the report should be amended in any way in response to the drop in markets caused by the Covid-19 pandemic. After consideration, the Actuary decided it was still appropriate to issue the report as it was, and also still appropriate to adjust Employer contributions. This was due to the Fund being a long term investor, holding assets for a long time, and not required to sell those equities that had dropped in value. It was anticipated that the value of equities, and therefore the Fund, would recover over time.

The Head of Pensions Governance and Investment also highlighted that membership of the Fund continued to increase steadily and overall membership was 71,500 at the end of the year. There were increases in every category of membership, although it was noted that over time the Fund was progressively maturing and there were more pensioners in relation to active members.

A Member queried the Committee attendance information which appeared incomplete and the Head of Pensions Governance and Investments agreed to investigate and ensure the final report was accurate.

ORDERED as follows:
1. The 2019/20 Annual Report and Accounts (Appendix A).
2. The Teesside Pension Fund Committee meeting attendance details would be updated.

20/14 **AUDIT PLANNING REPORT - ADDENDUM - YEAR ENDED 31 MARCH 2020 - JULY 2020**

The Teesside Pension Fund Audit Planning Report for the year ended 31 March 2020 was previously considered by the Committee at the March meeting. Since that Planning Report was prepared prior to the impact of the Covid-19 pandemic, an Addendum Report had now been submitted to update the Committee on how Covid-19 had impacted the External Auditors' risk assessment and the additional response which would be built into the audit as a result.

The External Auditor highlighted updates to two significant risks previously identified: the valuation of unquoted pooled investment vehicles and the valuation of directly held property.

The valuation of the Fund's investments in unquoted pooled investment vehicles had been identified as a significant risk, as even a small movement in the assumptions underpinning investment manager valuations could have a material impact on the financial statements. Unquoted assets were either Level 2 or Level 3 on the Fair Value Hierarchy, which meant that quoted market prices were not available and the valuation relied on the use of inputs derived from observable market data (Level 2) or were not based on observable market data (Level 3). The approach usually taken to value these assets had changed due to the market volatility brought about by Covid-19 in the final quarter of 2019/2020. Therefore the Auditor needed to consider the revised valuation approach taken by the Fund and its fund managers in order to gain assurance that the impact of Covid-19 on investment values had been properly accounted for in the financial statements.

Within the Fund's directly held property there were a number of retail property assets. Current market conditions in the retail sector meant that judgements and assumptions used to value these assets were also sensitive to market volatility. In line with guidance issued by the Royal

Institution of Chartered Surveyors (RICS), the Fund's Property Valuer had provided their valuation of the Fund's directly held property at 31 March 2020 on the assumption that there was a 'material valuation uncertainty' due to the impact of Covid-19 on the real estate market.

The Fund's directly held property were generally of a nature where the valuation uncertainty would be expected to be higher. The Auditor therefore considered the level of uncertainty around the Fund's property valuations to have increased. The Auditor stressed that the directly held property had previously been identified as a significant risk for the audit and therefore the additional uncertainty did not change the overall risk assessment. Management would need to include disclosures within the financial statements to inform users of the statements of the material valuation uncertainty. In addition, EY's property experts would review a larger number of individual property valuations to ensure that the additional uncertainty risks were adequately addressed.

The Auditor also highlighted other potential impacts of Covid-19 including: Going concern and post balance sheet event disclosures and changes introduced to EY's review and consultation procedures, further details of which were provided at page 7 of the submitted report.

Materiality levels for the audit were originally set at 1% of net assets as previously reported to the Committee. However, given the decrease in Fund asset values, the Auditor had considered whether 1% was still an appropriate threshold and was satisfied that it was. Materiality had therefore decreased from £40.8 million stated in the planning report and was now set at £37.4 million - 1% of the asset value in the draft Accounts. Performance materiality had been set at £28.0 million (previously £30.6m), which represented 75% of materiality. Finally, the threshold for audit differences had reduced from £2.0 million to £1.9 million.

In response to a query regarding the extra cost to the Fund of the additional procedures that the Audit would incur in providing additional work on the increased risks, the External Auditor stated that this would be discussed with management once the Audit was complete. The Head of Pensions Governance and Investments stated that the additional costs would be reported to the Committee.

ORDERED that the report was received and noted.