Report and Accounts

2001/02

Contents

Members of the Pensions Committee, Investment Managers, Advisors and Officers

Committee Members

Chairman	Councillor R. S. Haws, J.P.
Vice Chairman	Councillor S. Stratford
South Tyneside M.B.C.	Councillor T.A. Bamford Councillor E. Battye Councillor A. Frost Councillor J.F. Harper Councillor C. Tolson Councillor E.M. Gibson
Gateshead M.B.C.	Councillor D. Bollands (substitute – Councillor N. O'Neill)
Newcastle City Council	Councillor G. Bell (substitute – Councillor C. Gray)
North Tyneside M.B.C.	Councillor M. Green (substitute – Councillor M. Madden)
City of Sunderland Council	Councillor J. Heron (substitute – Councillor P. Young)
Trades Union Representatives	G. Clements – UNISON W. Flynn – UCATT S. Forster – UNISON

Investment Managers

Indexation	Legal and General Investment Management
Global Equities	Capital International
Emerging Market Equities	Capital International
Pan European Equities	UBS Global Asset Management
UK Equities	Fidelity Pensions Management
Far East Equities	Schroder Investment Management
Corporate Bonds	Prudential M&G
Global Government Bonds	Henderson Global Investors
Property Manager	Aberdeen Property Investors
Private Equity	HarbourVest
AVC Providers	Equitable Life Assurance Society The Prudential Assurance Company
Actuary and Investment Advisor	Watson Wyatt Partners
Executive Director Resources	J. Alderson
Head of Pensions	S. Moore
Head of Legal Services	C.G.D. Bradley
Pensions Manager	D. Smith
Loans and Investment Manager	I. Bainbridge

Vision Statement

Our goal is to provide an attractive and affordable pension arrangement that is seen by employers and members as an important and valued part of the employment package.

We will:

- ***Promote membership of the Fund.***
- ***Keep employers' contributions as low and as stable as possible through effective management of the Fund.***
- ***Work with our partners to provide high quality services to employers and members.***
- ***Make pensions issues understandable to all.***

We will know we are succeeding when:

- ***We are consistently achieving our investment objective.***
- ***There are sufficient assets to meet the liabilities, without a need for additional contributions from employers.***
- ***Employers and members tell us they are highly satisfied with the services we provide.***
- ***We are recognised as being amongst the leading UK pension funds.***

Introduction

I am pleased to introduce the 2001/02 Annual Report and Accounts for the Tyne and Wear Pension Fund.

For the second year running the world's equity markets have fallen in value. Despite this, strong relative investment performance meant that the Fund increased in value during the year, from £2,190 million to £2,214 million. The Fund's investment return for 2001/02 was a creditable +0.3%, which was 2.7% ahead of the Fund's benchmark and 1.9% ahead of the average UK pension fund.

The five year return of 7.3% per annum is 0.7% per annum ahead of the benchmark and 0.5% per annum above the return of the average UK pension fund. Pension fund returns are generally assessed over five year periods, therefore this performance is pleasing.

This strong performance has been achieved at a time when the Fund has undertaken a significant restructuring of its assets and investment management arrangements. The changes were driven by a desire to ensure that the Fund is properly positioned in relation to its liabilities and to future opportunities in investment markets. The restructuring raised turnover in assets during the year to £4.4 billion. It resulted in the termination of the appointment of three investment managers from the original nine, the appointment of three new managers and a changed role for a further four managers. Each manager in the new structure is a specialist in the market in which they invest.

If the relative investment performance was the good news for the year, the bad news was the fall in the funding level. The actuarial review of the Fund as at 31st March 2001 revealed that the funding level had fallen by 5% to 81.7%. The main reasons for this were the fall in world equity markets and the increased life expectancy of pensioners.

Communicating clearly and concisely with members is an important aspect of managing the Fund and we are continually looking to improve in this area. To assist us we survey members and ask them to express their views. We were pleased to hear that in our 2001/02 survey of pensioners 94% were satisfied with the service we provide. In the coming year we will survey our active members and ask them their opinion.

A significant event during the year was the Government's publication of a Code of Investment Principles. This was in response to an earlier review into institutional investment in the UK. The Principles cover issues such as effective decision making, setting clear objectives and performance measurement. The Fund already complied with many of these principles. A schedule on compliance is contained in the Report and Accounts.

Overall, this has been an extremely busy year for the Fund and 2002/03 is unlikely to be any different. Since the year-end equity markets have continued to fall. We will keep our investment strategy under close scrutiny as events develop.

Julie Alderson
Executive Director Resources

Fund Report

Administration

South Tyneside Metropolitan Borough Council is the administering authority for the local government pension fund for the Tyne and Wear County area. The Fund is set up in accordance with the provisions of the Local Government Pension Scheme.

The Council has established a Pensions Committee which is required to control and resolve all matters relating to the administration and investment of the Fund. The Committee consists of fifteen members. Eight of the members are nominated by South Tyneside and the other four district councils within the County area nominate one member each. Three representatives nominated by the trades unions also attend Committee meetings.

The Committee meets quarterly to consider all pension matters. Additional meetings are called should an aspect of the investment of the Fund require an in depth review. The Committee also has an annual meeting at which it considers the Report and Accounts.

Annual meetings are held for the trades unions whose members participate in the Fund and for employing organisations. The agenda for these meetings covers the actuarial position, investment performance and the benefits structure, and includes presentations by the Actuary and by an investment manager.

The Committee has an Investment Panel to provide a greater focus on, and scrutiny over, the performance and strategy of the investment managers. The Panel consists of three members of the Pensions Committee, the Actuary, the Executive Director Resources and the Head of Pensions. It meets in advance of the Committee and reports back on its findings and makes recommendations on any action that is required.

Membership

As at 31st March 2002, there were 101 employing bodies participating in the Fund. This includes the five district councils and a wide range of other organisations that provide a public service within the County area. These organisations are listed on pages 36 and 37.

Membership of the Fund has grown by 3,071 over the year, as set out below:

	2001/02	2000/01
Contributors	**44,585**	43,456
Deferreds	**13,170**	11,937
Pensioners	**27,291**	26,582
Total	**85,046**	81,975
Employers	**101**	95

Deferred members are either former employees who left their employing organisation before retirement age or employees who opted out of the Scheme whilst continuing to be employed. As and when they reach retirement, they are entitled to the payment of pension benefits based on their accrued service.

Communications Strategy with Fund Members

Membership of the Local Government Pension Scheme continues to be promoted as being in the best interests of local government employees.

The Fund aims to communicate with all members in a clear, concise and informative manner. The major features of our strategy are outlined below:

- A pensions telephone helpline.
- A Pension Fund Website.
- An annual benefit statement for all active members, direct to their home address. These statements were produced for the third year running, accompanied by a summarised version of the Report and Accounts and a newsletter.
- A letter to our pensioners detailing the annual increase to their pension, together with a summarised version of the Report and Accounts.
- Pensions seminars are provided to groups of members on request. Over 500 employees attended 29 seminars held at various employer locations throughout the year.
- A comprehensive range of information leaflets. These are provided in a variety of formats for people with special needs, such as large print, Braille and foreign languages.

The Fund is committed to continually improving communications with its members. To assist us in this process we contacted over 2,000 pensioners and asked them to comment on the service they receive. Over 1,000 pensioners responded and we were pleased to find that 94% declared they were satisfied with the service we provide.

In the coming year we intend to survey our active members and ask them to express their opinions.

Pension Fund Website for Members

Good progress has been made on the Fund's website during the year. This will become increasingly important to our service delivery package. Members now have access to:

- Latest news and topical issues.
- Other useful websites.
- Pensions Committee reports.
- Details on how to contact the Fund.
- Current and previous years Annual Report and Accounts.
- Details of the Fund's Statement of Investment Principles and Policy on Socially Responsible Investment, The Exercise of Rights and Corporate Governance.
- Scheme booklets.
- Pension payment dates and details of pension inflation proofing.
- Comment about the Fund.

The next phase of development is scheduled to commence in the near future. This will allow members to carry out the following on line:

- Request an estimate of benefits.
- Request information on increasing their standard benefit package.
- Change personal details.
- Request general information.

Over the longer term the Fund is looking to increase the interactive nature of the site. This will allow members to view their personal record and calculate estimates of existing benefits and possible improvements to their benefits.

The website address is **www.twpf.info**

Communications Strategy with Fund Employers

We aim to communicate effectively with the employers in the Fund. Our communications strategy includes the following:

- The Annual General Meeting.
- The provision of an Employers Guide to the administration of the Fund.
- Training courses that aim to educate and inform staff on pension matters and working procedures.
- The provision of a joint Memorandum of Understanding that sets out our respective roles and responsibilities.
- Regular mailshots and updates.
- The Pension Fund Website, which has a dedicated section for employers.
- Occasional meetings with liaison staff. We would like to develop a more regular programme of meetings for those employers that would value this.

Replacement Pensions Processing System

In February 2002, the Pensions Committee approved the award of a contract to Comino for a new pensions administration system.

We were the second local government fund to choose the Comino system. The new system will offer the flexibility and control needed to provide members and employers with the highest level of service and will also provide a platform for future development. In these times when service and accountability are of paramount importance, this new system will give us efficiency gains that will enable us to work towards the provision of Best Value.

We are currently carrying out the necessary development work to enable the new system to go live later in the year.

Legal Framework

The provisions of the Local Government Pension Scheme are contained in statutory regulations that are made by the Office of the Deputy Prime Minister and are ultimately approved by Parliament. These regulations apply nationally to all local authorities in England and Wales.

The Local Government Pension Scheme Regulations 1997, as amended, which were introduced with effect from 1st April 1998, set out the current rates of contribution and the method of calculation of benefits.

The legal framework for the investment of the Fund is set out in the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998, as amended. These regulations set out the types of investments which can be made, which include company and government securities, property and unit trusts, and set out restrictions on the proportion of the Fund which can be held in certain types of investment.

Amendments to the Local Government Pension Scheme Regulations 1997

The 1997 Regulations were modified during the year in order to improve and adapt them to meet new requirements.

The principal amendments include the following:

- A change to the way in which membership of the Scheme is calculated, both for establishing entitlement to benefit and in calculation of benefits.

- Fine tuning provisions dealing with ongoing access to the Scheme for staff involved with contracted out services and functions.
- Provision for some specific new bodies to have continued access to the Scheme for their employees.
- Changes required by other legislation, concerning the Pensions Advisory Service and deferment of annuity purchases.
- Amendments to reflect overriding European Law on Maternity and Paternity Leave.
- The reinstatement of the preserved right of retirement for pre-April 1998 members.
- Use of AVCs to purchase scheme benefits.

Employees' Contributions

The 1997 Regulations introduced a common contribution rate of 6% for all members. Manual workers who were members prior to 1st April 1998 have retained the right to pay 5% for as long as they remain in the Scheme.

Employers' Contributions and the Fund Valuation

Employees' contributions do not cover the total cost of the benefits. Employers participating in the Fund meet the balance of the cost with their contributions. The Fund's Actuary values the Fund every third year in order to assess each employer's share of the cost.

The employers' contributions for the 2001/02 year were set by the 1998 valuation. The 2001 valuation has now been completed and shows that, as at 31st March 2001, the funding level, which is the relationship between the assets and liabilities as at the valuation date, was 81.7%. This is a decrease of 5% from the level of 86.7% revealed by the 1998 valuation. This represents the average funding level across the Fund as a whole, with each participating employer having their own specific funding level. The strategy continues to be to make good this deficiency over a period of thirteen years.

The fall in the funding level is attributable to an increase in early retirements, the improved life expectancy of pensioners and, most importantly, the unfavourable performance of investment markets. Offset against this is the Fund's relatively good investment performance.

The 2001 valuation also identified the need to increase the future service contribution rates from 166% to 190%. This is the contribution required to meet the cost of the ongoing accrual of future benefits.

The next valuation of the Fund will take place as at 31st March 2004, with the resulting contribution rates taking effect from 1st April 2005.

Information on the actuarial position of the Fund and the employers' contributions is set out in the Actuary's reports, which are on pages 24 and 25.

Benefits

The Scheme provides an extensive range of guaranteed benefits for members and their dependants, including:

- A pension and tax free lump sum on retirement.
- Widows' and widowers' benefits.
- Children's pensions.
- Index-linking of all pensions.

- A lump sum on death in service (and sometimes on death after retirement).
- Transfer values to other pension arrangements or index-linked preserved benefits for early leavers.
- A refund of contributions where no other benefit is due.
- Facilities for paying additional contributions to provide additional benefits.

Additional Voluntary Contributions

Whilst the Local Government Pension Scheme provides an excellent benefits package, it is normally possible to increase benefits and thereby take full advantage of the tax relief which is available. This can be done either by purchasing added years of service within the Scheme or by paying into an Additional Voluntary Contributions (AVC) plan.

As well as allowing members to boost their pension up to the maximum allowed under Inland Revenue rules, AVC plans can also be used to provide extra life assurance.

We have AVC plans arranged with Equitable Life and The Prudential. The Fund no longer promotes the scheme operated by Equitable Life, although it is not formally closed. Members may choose to invest with either company, but Equitable Life's problems have meant that almost all new investors are now choosing The Prudential.

Equitable Life continues to experience financial difficulties. The obligations that arose from some of its financial products that carry guaranteed returns, which primarily affect its With-Profits Fund, have now been alleviated by a compromise deal. However, poor stockmarket performance over the last two years has reduced reserves and forced significant bonus reductions. Although certain elements of Equitable Life have been sold to the Halifax, the With-Profits Fund remains with Equitable Life.

Whilst Equitable Life remains solvent and continues to pay out benefits, the Society has actioned the following:

- Due to poor investment returns, no interim bonus will be applied for 2002. The position will be reviewed during the year.
- The current Board has suggested that it inherited a "unique and unsatisfactory" bonus methodology. Equitable Life intends to adopt a policy similar to that of other providers in the future.
- To reflect the above change, maturity policy values for retiring members were reduced by 4% from the 15th April 2002. The reduction was then increased to 10% from the 1st July 2002. Maturity values will not, however, be less than the guaranteed value of the policy. The purpose of this change in the calculation is to ensure that those leaving the With-Profits Fund do not leave with more than their fair share.
- The Market Value Adjustment that applies to individual and group early withdrawals from the With-Profits Fund increased from 10% to 14% on 15th April 2002, then to 20% on 1st July 2002.
- Equitable Life is to launch legal proceedings against the Society's former auditor, Ernst and Young. It will also be investigating the possibility of proceedings against some former directors.

The situation regarding Equitable Life has been very difficult for the Fund. We are continually monitoring the position of our members' AVC investments and trying to establish the best way forward. We are taking regular advice from our legal and investment advisers and continue to keep members informed of any new developments as they arise.

Stakeholder Pensions

Stakeholder pensions were introduced on 6th April 2001 and are intended to provide a low cost, privately funded, supplement to the basic state pension.

Since October 2001, all employers that do not already offer a pension scheme must provide access to a stakeholder scheme for their employees.

Although most employers participating in the Tyne and Wear Pension Fund are not subject to this requirement, many of our members can contribute to a stakeholder pension scheme as well as to the Local Government Pension Scheme. This is because the Government has allowed those occupational pension scheme members with earnings of less than £30,000 p.a. to make further contributions to a stakeholder scheme.

Pension Rights for Part Timers

The Local Government Pension Scheme currently offers membership to all employees regardless of the number of hours worked. However, prior to January 1993 some part time employees were excluded from membership.

The House of Lords has since ruled that such employees suffered from discrimination and can backdate their membership as far back as 8th April 1976. This will only be permitted where the appropriate pension contributions are paid.

Any employees who believe they are affected by this judgement and who would like to secure Scheme membership must pursue their claim through an employment tribunal. If they have left employment or have changed job, their claim must have been registered within six months of leaving. These tribunals are currently "stayed" pending the outcome of a number of test cases.

The results of the test cases are currently under consideration and the Local Government Pension Scheme Regulations may be amended to cover this situation.

Local Government Pension Scheme - Stocktake Exercise

Ministers agreed in July 2001 to authorise a stocktake of the Scheme as part of the Office of the Deputy Prime Minister's stewardship responsibilities. Assessments of this kind are undertaken to ensure that the Scheme is operating effectively, efficiently and that it continues to provide value for money.

The Office of the Deputy Prime Minister has published a paper aimed at fostering discussion of a range of options for the future of the Scheme. The aim of this is to provide local government employees with a scheme which is more suitable for modern working trends.

The discussion paper suggests that the present Scheme is a reasonable scheme for many employees who stay in local government throughout their career, but does not serve so well the pension needs of others such as part-timers, careerbreak employees, low paid workers and contract workers.

The discussion paper makes it clear that the present Scheme is not being challenged. Thoughts are invited on a number of possible elements of change, such as:

- The scope for further simplification of the Scheme's legal framework, particularly within the context of the recommendations from the Pickering Review being conducted on private sector pension legislation.
- An assessment of the options from which it may be possible to develop a more flexible Scheme benefit package for new employees from a future date.
- Establishment of measures to enhance the Scheme's benefit administration capacity in order to ensure the cost-effective delivery of a quality service.
- Establishing new means to monitor all the factors which influence the Scheme's on-going sustainability on a fund-by-fund basis.

This review follows a similar exercise for the civil service scheme. Reviews of other public service pension schemes may well follow.

Investment Report

Investment Objectives

The formal investment objectives of the Fund are:

- To maintain securely a portfolio of assets of appropriate liquidity which will generate income and capital growth which, together with employer and employee contributions, will meet the cost of current and future benefits which the Fund provides, as set out in the relevant statutory documentation.
- To minimise the long term costs of the Fund by maximising the return on the assets, whilst having regard to the objective set out above.
- To comply with the regulations relating to the investment of local government pension funds.

Investment Policy

The Fund's investment policy has been reviewed following the completion of an asset liability study. This study examined the Fund's financial position, the profile of its membership, the nature of its liabilities and included an analysis of the expected returns from differing investment policies.

Having considered the outcome of the study, the Pensions Committee concluded that a diversified portfolio, of which 65% is invested in Equities and 35% is invested in Bonds and Property, would represent a suitable strategic benchmark for the Fund. The new benchmark is shown in the following table:

Asset Class	Strategic Benchmark %
UK Equities	**30.00**
Overseas Equities	
- US	9.75
- Europe ex UK	12.25
- Japan	6.50
- Other Far East	3.25
- Emerging Markets	3.25
Total Overseas Equities	**35.00**
Total Equities	**65.00**
Fixed Interest	
- UK Gilts	8.75
- UK Index-Linked	5.00
- Sterling Non Government	11.00
- Overseas	2.75
Total Fixed Interest	**27.50**
Property	**7.50**

Prior to the changes, the Fund's benchmark was represented by the average or consensus asset allocation within the Russell/Mellon CAPS survey. Whilst this has provided an appropriate benchmark for the Fund for a number of years, it was becoming clear that its suitability was diminishing as a number of other funds moved to fund specific benchmarks.

The new strategic benchmark has not resulted in a significant change to the overall allocation to Equities. However, there was a move into UK Fixed Interest and Overseas Equities at the expense of UK Equities, Overseas Fixed Interest and Cash. Over time, there will also be an increased allocation to Private Equity.

The move to the new benchmark was largely completed by the 31st March 2002, although the final stages of the transition were not undertaken until after the year-end. The new strategic policy benchmark was fully operational from 1st July 2002.

The Pensions Committee will continue to monitor the suitability of this policy in the light of the Fund's developing liabilities and finances.

Investment Management Structure

Changes have been made to the investment management structure in order to ensure that the policy and the structure complement one another.

Prior to the changes, half of the Fund was managed on a balanced basis and half on a specialist basis. At this time, the following managers were employed by the Fund:

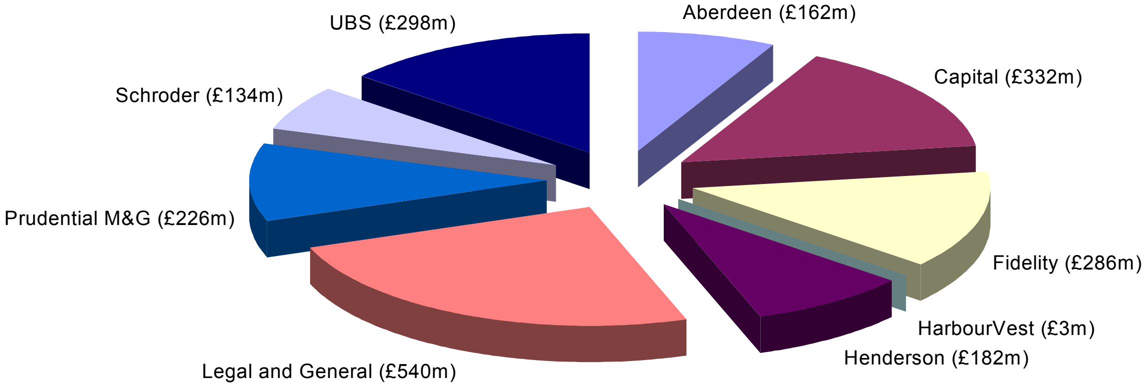
Manager	Portfolio
UBS	Balanced
Fidelity	Balanced
BGI	UK Equities Indexed
Morley	UK Equities Active
JP Morgan	US Equities
Capital	European Equities
Schroder	Far East Equities
Prudential M&G	Global Bonds
Aberdeen	Property

The review of the management structure resulted in a move away from balanced management. Under the new structure, the Fund employs nine managers over a total of fourteen investment mandates. Each manager is a specialist in the market in which they invest. This broadly based management structure ensures that investment returns are not overly influenced by the performance of any one manager.

The new structure is set out in the following table:

Manager	Portfolio
Legal and General	Indexation - UK Equities - US Equities - Corporate Bonds - UK Index-Linked
Capital	Global Equities Emerging Market Equities
UBS	Pan European Equities
Fidelity	UK Equities
Schroder	Far East Equities
Prudential M&G	Corporate Bonds
Henderson	Global Government Bonds
Aberdeen	Property
HarbourVest	Private Equity

The value of assets with each manager at the year-end is shown below:



Investment Managers' Objectives and Restrictions

The Pensions Committee has set objectives and restrictions for the investment mandates. These have been prepared with the aims of ensuring a prudent approach to investment and of allowing each manager to implement their natural investment style and process.

In addition to the specific restrictions on each mandate, all managers are required to comply with the requirements of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998, as amended.

The managers have been set targets, based on an appropriate index, which require outperformance over three year rolling periods. Annual downside targets have also been set.

In addition to managing a range of indexed portfolios on behalf of the Fund, Legal and General assists the Fund's officers to maintain the asset allocation of the Fund in line with the strategic benchmark.

Investment in Private Equity will be made largely on a fund of funds basis. Whilst an outperformance target relative to quoted equity markets has been set, official measurement against this is not appropriate at this early stage of investment into this asset class.

The Property Portfolio, which is managed by Aberdeen Property Investors, has a target based on the Investment Property Databank (IPD) Index. Aberdeen is also responsible for advising the Committee on the proportion of the Fund's assets which should be invested in Property.

Custodians

When appointing an investment manager, the Committee is prepared to appoint that manager's in-house or recommended custodian to act as custodian for those assets under management, providing that criteria on security of assets and service standards can be met. Where a manager does not recommend a custodian, the Committee will make the appointment. Under the new management structure there are four investment managers who do not recommend a custodian. Consequently, following a tender exercise, the Fund appointed Northern Trust to act as custodian for these managers. The custodians for each manager are noted below:

Manager	Custodian
Legal and General	Northern Trust
Capital	Northern Trust
UBS	UBS
Fidelity	Northern Trust
Schroder	Schroder
Prudential M&G	Boston Safe Deposit and HSBC
Henderson	Northern Trust

Investment Strategy and Performance

Strategy

The Fund's overall asset allocation is set in line with the strategic benchmark. The asset allocation is maintained within pre-determined ranges around the strategic benchmark. When a range is breached, the Fund is rebalanced back to the benchmark weightings.

Managers who invest in more than one market have the ability to make tactical asset allocation decisions within their own portfolios. This does not impact on the Fund's overall strategy, but does provide additional scope for managers to outperform their targets.

The exposure to Private Equity will be built up to approximately 5% of the Fund over a period of time. This will be top sliced from the overall equity weighting.

The tactical allocation to Property is set by the Pensions Committee, based on recommendations from the Property Manager and advice from the Actuary.

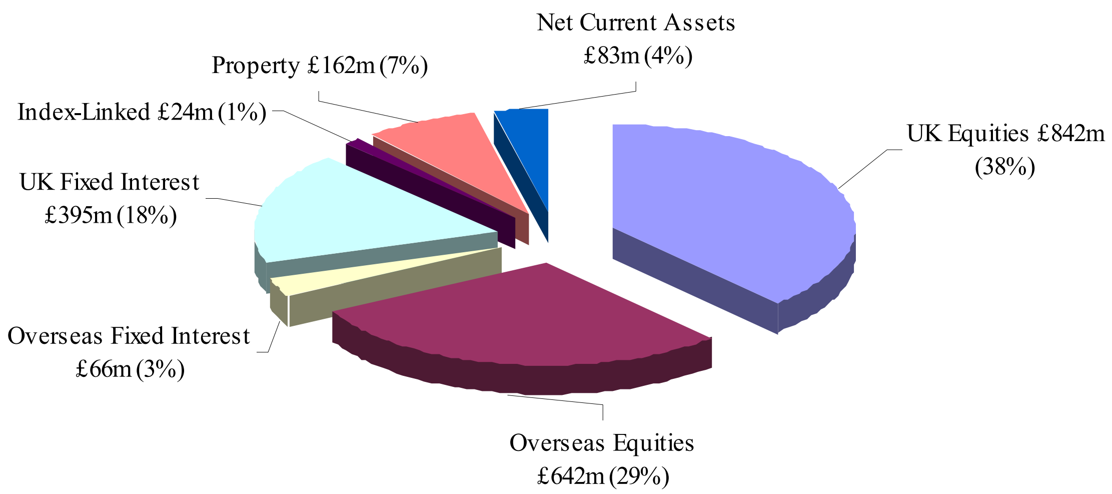
As at 31st March 2002, the Fund's move to the new strategic benchmark was largely complete. The final stages of this transition took place in the first quarter of 2002/03 with an injection into Overseas Equities and Index-Linked Bonds at the expense of Cash and UK Equities.

The change to the asset allocation during the year, including the impact of market movements, is illustrated in the following table:

Asset Class	%	£m
UK Equities	-9.5	-199
Overseas Equities	+12.1	+272
UK Fixed Interest	+10.6	+238
Overseas Fixed Interest	-6.6	-145
Index-Linked	-0.8	-17
Property	+0.2	+6
Net Current Assets	-6.0	-131

Tyne and Wear Pension Fund

The asset allocation as at 31st March 2002 is shown below:



Performance Measurement

One of the consequences of moving to a new strategic benchmark is that, going forward, performance will no longer be measured against the median pension fund. A fund specific benchmark based on the strategic asset allocation will be used in its place.

For all periods ending on 31st March 2002, a hybrid performance benchmark has been used. This is based on the median up to and including the first ten months of 2001/02 and a fund specific benchmark for the final two months.

Returns for 2001/02

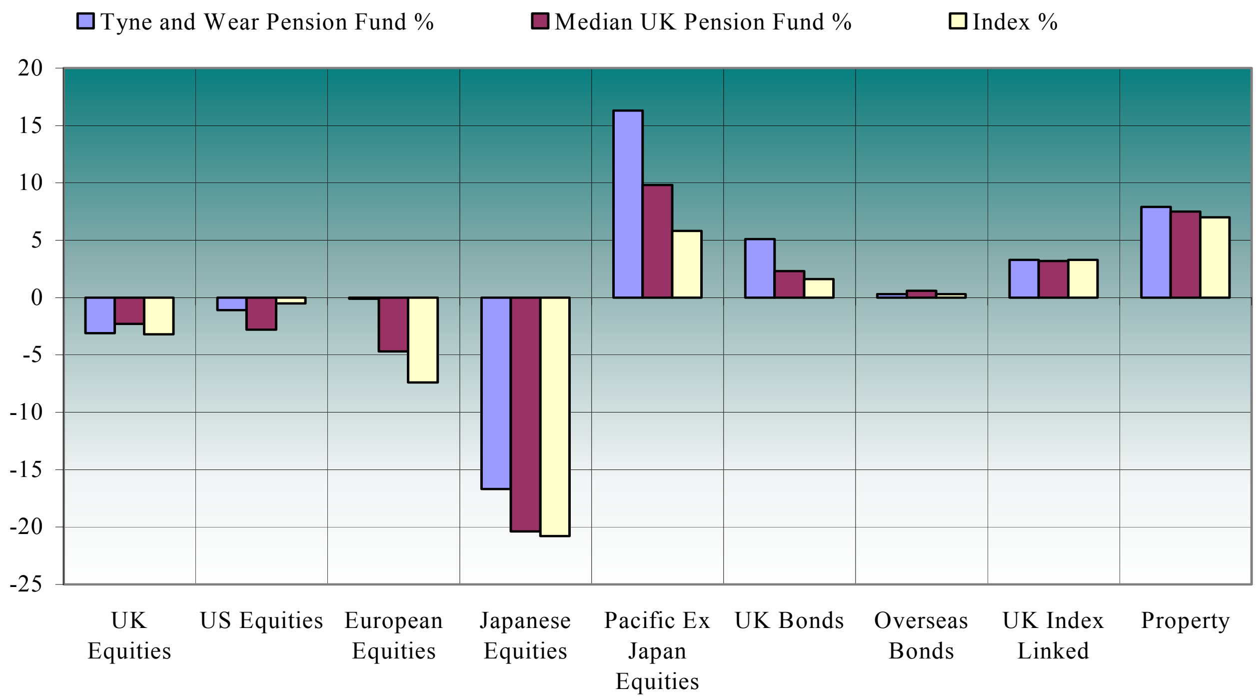
The Fund's investment return for the year was 0.3%. This return was very satisfying in the light of market conditions and the fact that the Fund was involved in a significant restructuring during the year. It was 2.7% ahead of the Fund's benchmark return for the year of -2.4% and 1.9% ahead of the return of the median pension fund, which was –1.6%.

Whilst the events of September 11th produced a sharp fall in equity markets and a slowdown in the global economy, the weakness in markets and the economic slowdown were already evident before this date.

In this environment the defensive nature of Cash, Property and Bonds meant that they all performed relatively strongly. Equities performed poorly, with markets in most regions falling. An exception to this was Pacific Rim ex Japan Equities which produced a return of nearly 6%.

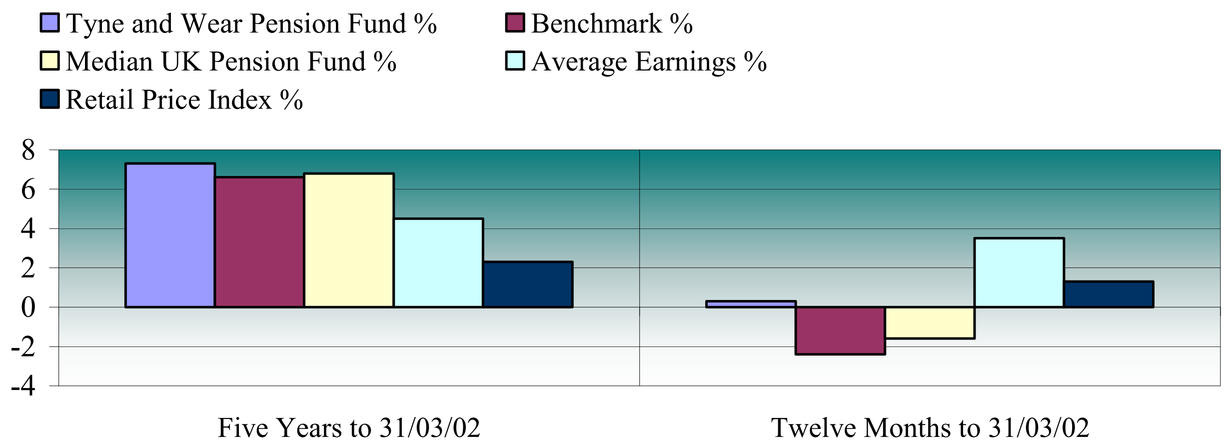
Tyne and Wear Pension Fund

The chart below shows the Fund's return over the main investment markets for 2001/02 and compares it against the median and index returns.



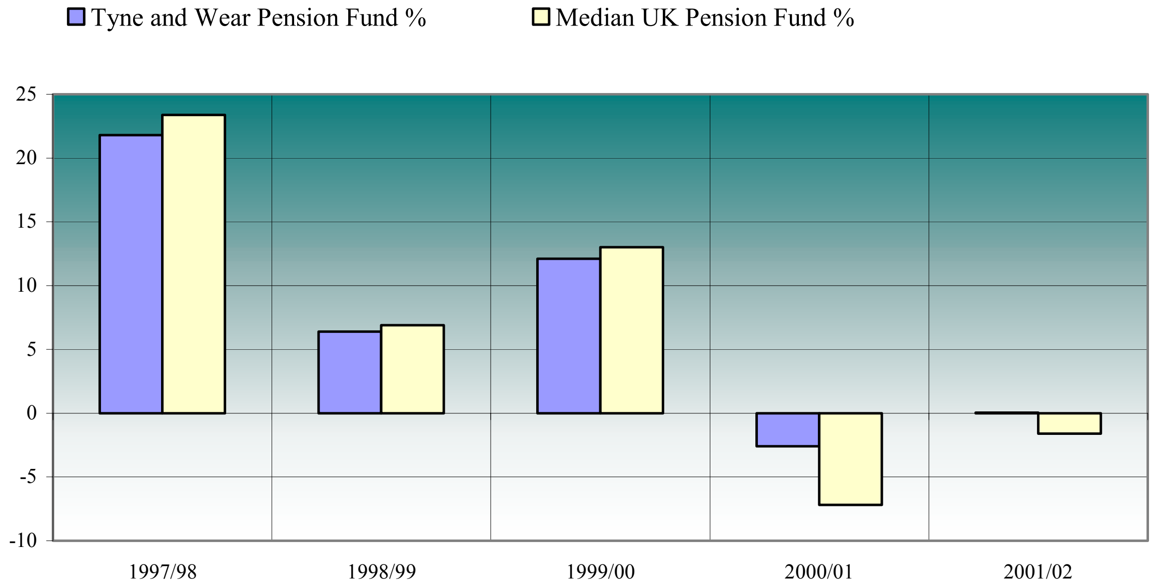
Five Year Performance

In order to avoid taking too short term a view of investment performance, pension fund returns are generally assessed over five year periods. This Fund's average annual return over the last five years has been 7.3% p.a. This was 0.7% above the Fund's benchmark return of 6.6 % p.a. and 0.5% p.a. above the median pension fund return of 6.8% p.a. It was also comfortably above the rate of inflation and the increase in wages over the period, as shown below:



Tyne and Wear Pension Fund

The annual performance relative to the median pension fund over the five year period is shown in the following chart:



For almost all of this five year period, the Fund has had a defensive asset allocation. This was mainly because of the investment views of UBS Global Asset Management (formerly Phillips and Drew), who used to manage the largest single portfolio in the Fund under the previous investment management structure. During the first three years of the period, financial markets performed very strongly and the defensive stance adopted by this manager detracted from returns. However, in 2000/2001 the market environment changed considerably with equity markets falling in value. The fall in equity markets continued into 2001/02. In this environment, the Fund and UBS performed extremely well in relative terms and more than reversed the losses of the earlier years.

Investment Markets after 31st March 2001

Since the end of the financial year, world Equity markets have fallen by approximately 30% due to concern about the global economy and fears over a war between the West and Iraq.

During this period, the Fund has fallen in value by about 18%. It has been protected from the worst of the falls in Equity markets by its exposure to Bonds and Property. We will keep our investment strategy under close scrutiny as events develop.

Investment Policies

Myners Report

In March 2000, the Chancellor of the Exchequer commissioned a review into institutional investment in the UK. He invited Paul Myners of Gartmore Investment Management to lead the review.

One year later, on 6th March 2001, the "Myners Report" was produced. In October 2001, the Government published a Code of Investment Principles that reflected the proposals of the Myners Report. There are ten Principles contained in the Code and, whilst compliance is currently voluntary, legislation has recently been introduced which requires local government pension funds to state the extent to which they are complying with the Principles.

A summary of these Principles and the Fund's compliance is shown below:

Principle 1 - Decisions should only be taken by those with sufficient expertise.	Partial Compliance. The only omission is the provision of a handbook to each Committee member containing terms of reference, standing orders and operational procedures.
Principle 2 – Clear investment objectives should be set.	Fully Compliant.
Principle 3 – Strategic asset allocation decisions should receive sufficient attention.	Fully Compliant.
Principle 4 – Contracts for actuarial services and investment advice should be open to separate competition.	Under consideration.
Principle 5 – An explicit written mandate should be agreed between the Fund and the investment managers and transaction related costs should be monitored.	Partial Compliance. Consideration is currently being given to improving the monitoring of transaction related costs.
Principle 6 – The Fund should play an active role in Corporate Governance.	Fully Compliant.
Principle 7 – The Fund should set appropriate investment benchmarks.	Fully Compliant.
Principle 8 – Arrangements should be made to measure the performance of the Fund, the Committee, advisers and managers.	Partial Compliance. The approach to a formal assessment of decisions taken by the Committee and the adviser is under consideration.
Principle 9 – The Statement of Investment Principles should be strengthened.	Fully Compliant.
Principle 10 – The Fund should publish its Statement of Investment Principles and the results of monitoring.	Fully Compliant

The Statement of Investment Principles

The Pensions Committee first approved a Statement of Investment Principles (SIP) in October 1997. At this time, the legal requirement to have such a document applied only to private sector schemes, but it was considered to be good practice for local government funds to prepare one.

With the introduction of the Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 1999, the need to produce a SIP was extended to local government funds. The latest version of the SIP was agreed in September 2002. It has been strengthened to comply with the requirements of the Myners Principles and Regulations, which require that the SIP should set out:

- Who is taking which decisions and why this structure has been selected.
- The Fund's investment objective.
- The Fund's planned asset allocation strategy, including projected investment returns on each asset class, and how the strategy has been arrived at.
- The mandates given to all advisers and managers.
- The nature of the fee structures in place for all advisers and managers and why this set of structures has been selected.
- The extent to which the Fund complies with the Myners Principles.

As would be expected, the contents of the SIP reflect the detail contained in this Annual Report and Accounts. A copy of the SIP is shown on pages 38 to 48.

Corporate Governance and Voting

The Pensions Committee believes that good corporate governance and the informed use of voting rights are an integral part of the investment process, which should improve the long term performance of the companies in which the Fund is invested. Voting rights are regarded as an asset that needs managing with the same duty of care as any other asset. The use of these rights is essential to protect the interests of the organisations participating in the Fund and the beneficiaries of the Fund.

It is important that this process is carried out in an informed manner and, for this reason, the Committee believes that the Fund's investment managers are best placed to undertake it.

The Committee requires each manager to prepare a document that sets out their policy on corporate governance and on the use of voting rights.

This policy has to provide for:

- The approach towards UK quoted companies to take account of the strong guidance offered by the Combined Code produced by the Hampel Committee.
- The approach towards companies outside the UK to take account of the practices of the home nation.
- Voting rights to be exercised in a manner which establishes a consistent approach to both routine and exceptional issues, in order that company directors fully understand the manager's views and intentions.

Whilst the Committee requires each manager to exercise voting rights in accordance with their individual policy, it retains the right to direct the manager in respect of any particular issue, should such action be considered appropriate.

Each manager is required to:

- Report any material change to their policy immediately.

- Provide an annual report which sets out their policy and the manner in which it has been implemented.
- Provide a quarterly report which sets out their voting record.

Socially Responsible Investment (SRI)

The Fund's SIP covers the extent to which social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments. This area is known as Socially Responsible Investment (SRI).

The policy on SRI requires that each manager must:

- Develop and co-ordinate policies on SRI, corporate governance and voting.
- When buying and selling investments, take into account how SRI factors might affect their value.
- For each company in which they invest, review that company's approach to social, environmental and ethical factors and, where necessary, approach company management to seek improvements.

This policy was reviewed and updated by the Pensions Committee in May 2002. A copy is shown on pages 49 to 50.

SRI is an important issue and the Pensions Committee takes its responsibility in this area very seriously. Investment managers are required to report on the implementation of this policy in their quarterly performance report and it is on the agenda for all meetings with investment managers.

Actuarial Information

Introduction

The Regulations require that an actuarial valuation is carried out every third year. The purpose of this is to establish that the Fund is able to meet its liabilities to past and present contributors.

Actuarial Position

1. Rates of contributions paid by the participating employers during 2001/02 were based on the actuarial valuation carried out as at 31 March 1998.

2. This valuation showed that the required level of contributions to be paid to the Fund by participating employers (in aggregate) with effect from 1 April 1999 was as set out below:

- 166% of members' contributions to meet the liabilities arising in respect of service after the valuation date.

Plus

- 75% of members' contributions over a period of 13 years (the members' average future service lifetime) to reflect the shortfall of the Fund's assets over 100% of its accrued liabilities, allowing, in the case of members in service, for future pay increases.

3. The contributions actually required from each participating employer over the period 1st April 1999 to 31st March 2002 are set out in a certificate appended to a seperate report on the actuarial valuation.

4. The market value of the Fund's assets at the valuation date was £1,858 million and the actuarial value of £1,618 million represented 86.7% of the Fund's accrued liabilities, allowing for future pay increases.

5. The contribution rates have been calculated using the projected unit actuarial method and the main actuarial assumptions were as follows:

Rate of return on investments:	7½% per annum
Rate of general pay increases:	5¼% per annum
Rate of increases to pensions in payment (in excess of GMPs):	3½% per annum
Valuation of assets:	discounted value of future income, based on an asset model of 50% in UK equities and 50% in index-linked gilts, assuming that that part of the assets notionally reinvested in the FT All-Share Index will achieve 4½% per annum dividend growth.

Report of the Actuary
For The Year Ended 31st March 2002

The last full actuarial investigation into the financial position of the Tyne and Wear Pension Fund in accordance with Regulation 77(1) of the Local Government Pension Scheme Regulations 1997 was completed as at 31st March 2001. The results showed that the financial position of the Fund had deteriorated since the previous valuation with the assets covering 81.7% of the liabilities, allowing for future pay increases in pensionable remuneration.

We recommended revised rates of contributions to be paid by the participating employers with effect from 1st April 2002. A formal Certificate of these contribution rates to be paid from 1st April 2002 was issued to the Director of Finance of the South Tyneside Metropolitan Borough Council as part of our formal report on the valuation of the Fund as at 31st March 2001.

Having regard to the results of the actuarial valuation as at 31st March 2001 and the rates of contribution in payment from 1st April 2002, together with the stepped increases recommended to apply in future years, the assets of the Fund as at 31st March 2002 will be sufficient, on the basis of the assumptions adopted for the valuation as at 31st March 2001, to meet the on-going liabilities of the Fund under the Regulations associated with both the accrued service and the currently accruing service, increasing levels of pensionable remuneration and increases to pensions both in payment and in deferment, taking into account the gradual amortisation of the deficiency disclosed by the valuation as at 31st March 2001.

The next actuarial valuation of the Pension Fund will be carried out as at 31st March 2004 and the results will be reported in the accounts for the year ending 31st March 2005, although the contribution rates found to be required as part of that valuation become effective from 1st April 2005.

R G Ashurst

Fellow of the Institute of Actuaries
Watson Wyatt Partners

Financial Statements

Fund Account

2000/01 £'000	2000/01 £'000		Note	2001/02 £'000	2001/02 £'000
		Contributions and Benefits			
114,050		Contributions Receivable	3	132,993	
18,940		Transfers In	4	11,822	
	132,990				144,815
96,799		Benefits Payable	5	102,764	
9,323		Leavers	6	20,152	
1,556		Administrative Expenses	7	1,925	
	107,678				124,841
	25,312	**Net Additions from Dealings with Members**			19,974
		Returns on Investments			
76,070		Investment Income	8	71,316	
-3,482		Non-Recoverable Tax	8	-4,773	
-130,490		Change in Market Value of Investments	9	-58,549	
-3,303		Investment Management Expenses	10	-3,771	
	-61,205	**Net Returns on Investments**			4,223
	-35,893	**Net Increase in the Fund During the Year**			24,197
	2,226,150	**Net Assets of the Fund at 1st April**			2,190,257
	2,190,257	**Net Assets of the Fund at 31st March**			2,214,454

Financial Statements

Net Assets Statement

2000/01			Note	2001/02	
£'000	£'000			£'000	£'000
		Investments	9		
259,544		Fixed Interest Securities		**185,310**	
1,291,103		Equities		**989,135**	
38,494		Index-Linked Securities		**24,275**	
235,547		Managed and Unitised Funds		**774,134**	
152,498		Properties		**158,800**	
205,450		Cash Deposits		**67,454**	
-6,584		Other Investment Balances		**2,208**	
	2,176,052				**2,201,316**
	14,205	**Current Assets and Liabilities**	11		**13,138**
	2,190,257	**Net Assets of the Fund At 31st March**			**2,214,454**

Notes to the Financial Statements

1. Basis of Preparation

The financial statements have been prepared in accordance with the main recommendations of the Statement of Recommended Practice, Financial Reports of Pension Schemes and follow the 2000 Code of Practice on Local Authority Accounting issued by the Chartered Institute of Public Finance and Accountancy.

The financial statements summarise the transactions of the Fund and deal with the net assets at the disposal of the Council. They do not take account of obligations to pay pensions and benefits that fall due after the end of the Fund year. The actuarial position of the Fund, which does take account of such obligations, is dealt with in statements prepared by the Actuary, which are detailed on pages 24 and 25. The financial statements should be read in conjunction with the Actuary's statements.

2. Accounting Policies

Acquisition Cost of Investments

The acquisition cost of investments is based on the purchase price plus any additional costs associated with the purchase.

Valuation of Investments

Quoted securities have been valued at their mid-market closing price on 28th or 29th March 2002. The 31st March 2002 was a non-business day and therefore the valuations are based on the closing price on the last business day of the reporting period.

Unitised securities have been included at the average of their bid and offer prices on 28th March 2002.

Other unquoted investments have been valued with regard to latest dealings and other appropriate financial information.

Overseas investments and foreign currency balances have been converted into Sterling at the closing exchange rates on 28th March 2002.

Properties are shown as valued at 31st December 2001. The valuers are Fellows of the Royal Institute of Chartered Surveyors from Drivers Jonas.

Investment Transactions

Investment transactions that were not settled as at 31st March 2002 have been accrued.

Investment Income

Investment income has been credited to the Fund on the ex-dividend date and is grossed up to allow for recoverable and non-recoverable tax. Non-recoverable tax has been shown as an expense.

Foreign income received during the year has been converted into Sterling at the exchange rate at the date of transaction. Amounts outstanding at the year-end have been valued at the closing exchange rates on 28th March 2002.

With regard to property rental income payable quarterly in advance, only the proportion of each payment attributable to the Fund from the due date to the 31st March 2002 is credited to the Fund Account.

Interest on cash deposits has been accrued up to 31st March 2002.

Investment Management Expenses

Investment management expenses payable as at 31st March 2002 have been accrued.

Debtors and Creditors

For Fund transactions, a system of income and converted payments is operated. Unless stated below, at the year-end, payments are converted to expenditure by the addition of unpaid creditors as at 31st March 2002. The accrual concept is in accordance with SSAP 24.

Contributions

Contributions represent the amounts receivable from the organisations participating in the Fund; these may be district councils, other scheduled bodies or admitted bodies. Such amounts relate both to their own employer contributions and to those of their pensionable employees. The rate for employers is determined by the Actuary. Contributions due as at 31st March 2002 have been accrued.

Benefits, Refunds and Transfer Values

Benefits and refunds are accounted for in the year in which they become due for payment. Transfer values are accounted for on a payments/receipts basis since not only do they frequently apply to several past years but, in the case of transfer values due, information is not available at the year-end on which to make an accrual.

3. Contributions Receivable

	2001/02 £'000	2000/01 £'000
Employers		
Normal	64,753	58,631
Additional	31,155	20,758
Members		
Normal	37,081	34,660
Additional Voluntary Contributions	4	1
	132,993	114,050

4. Transfers In

During the year, individual transfers in from other schemes amounted to £11.822 million (£18.940 million in 2000/01).

5. Benefits Payable

	2001/02 £'000	2000/01 £'000
Pensions	94,615	88,754
Commutations and Lump Sum Retirement Benefits	15,063	15,088
Lump Sum Death Benefits	2,356	1,563
Less: Recharges	-9,270	-8,606
	102,764	96,799

6. Payments to and on Account of Leavers

	2001/02 £'000	2000/01 £'000
Individual Transfers to Other Schemes	19,716	8,958
Refunds to Members Leaving Service	436	365
	20,152	9,323

7. Administration Expenses

The Local Government Pension Scheme Regulations 1997 permit costs incurred in connection with the administration of the Fund to be charged against the Fund. A breakdown of the costs is set out in the following table:

	2001/02 £'000	2000/01 £'000
Employee Expenses	961	909
Support Services Recharge	721	509
External ICT Costs	102	154
Printing/Publications	40	80
Actuarial Fees	133	40
Other Expenses	73	78
SIB Pension Review	-68	-178
Other Income	-37	-36
	1,925	1,556

Employee expenses have been charged to the Fund on a time basis. Office expenses and other overheads have also been charged.

8. Investment Income

	2001/02 £'000	2000/01 £'000
Fixed Interest Securities	18,660	15,855
Equities	31,660	35,418
Index-Linked Securities	686	1,460
Managed and Unitised Funds	3,225	2,803
Properties – Net Rents	10,968	10,233
Cash Deposits	6,116	10,298
Underwriting Commission	1	3
Sub-Total	71,316	76,070
Less: Non-Recoverable Tax	-4,773	-3,482
Total Investment Income	66,543	72,588

9. Investments

	Value at 1.4.01 £'000	Purchases at Cost £'000	Sales Proceeds £'000	Change in Market Value £'000	Value at 31.3.02 £'000
Fixed Interest Securities	259,544	562,245	-634,160	-2,319	185,310
Equities	1,291,103	826,813	-1,061,786	-66,995	989,135
Index-Linked Securities	38,494	28,291	-43,034	524	24,275
Managed and Unitised Funds	235,547	795,789	-264,811	7,609	774,134
Properties	152,498	12,923	-7,750	1,129	158,800
	1,977,186	2,226,061	-2,011,541	-60,052	2,131,654
Cash Deposits	205,450	0	-139,079	1,083	67,454
Other Investment Balances	-6,584	-3,084	11,456	420	2,208
	2,176,052	2,222,977	-2,139,164	-58,549	2,201,316

The change in market value of investments during the year comprises all increases and decreases in the market value of investments held at any time during the year, including profits and losses realised on sales of investments during the year.

		2001/02 £'000	2000/01 £'000
Fixed Interest Securities			
UK Public Sector		69,036	74,353
UK Other		49,848	6,906
Overseas Public Sector		66,426	177,750
Overseas Other		0	535
		185,310	259,544
Equities			
UK Quoted		415,793	1,003,024
UK Stock Index Futures		0	1,749
UK Unquoted		159	13
Overseas Quoted		570,468	286,317
Overseas Unquoted		2,715	0
		989,135	1,291,103
Index-Linked Securities			
UK Quoted		24,275	3,378
Overseas Quoted		0	35,116
		24,275	38,494
Managed and Unitised Funds			
UK Managed Funds	- Other	721,727	206,863
Overseas Managed Funds	- Other	42,986	0
UK Unit Trusts	- Property	3,100	3,462
	- Other	6,315	23,948
Overseas Unit Trusts	- Other	6	1,274
		774,134	235,547
Properties			
Freehold		124,050	130,223
Long Leasehold		34,750	22,275
		158,800	152,498
Cash Deposits			
Sterling		65,833	200,628
Foreign Currency		1,621	4,822
		67,454	205,450
Other Investment Balances			
Cash Backing Open Stock Index Futures		0	-1,749
Currency Hedging		251	-96
Debtors		15,597	15,659
Creditors		-13,640	-20,398
		2,208	-6,584

10. Investment Management Expenses

The Local Government Pension Scheme Regulations 1997 permit costs incurred in connection with the investment of the Fund to be charged against the Fund. A breakdown of the costs is set out below.

	2001/02 £'000	2000/01 £'000
Administration, Management and Custody	3,549	3,170
Performance Measurement Services	43	50
Other Advisory Fees	154	71
Audit Fees	25	12
	3,771	3,303

Administration includes employee expenses that have been charged to the Fund on a time basis. Office expenses and other overheads have been charged.

11. Current Assets and Liabilities

	2001/02 £'000	2000/01 £'000
Contributions and Recharges Due	10,949	9,135
Dividend Accruals	4,760	7,760
Recoverable Taxation	522	285
Inland Revenue	-1,533	-1,401
Investment Management Expenses	-1,515	-869
Other	-45	-705
	13,138	14,205

12. Analysis of Investments over Fund Managers

The market values of investments in the hands of each manager were:

As at 31st March 2001 £'000	%		As at 31st March 2002 £'000	%
156,005	7	Aberdeen Property Investors	162,012	7
422,481	19	Barclays Global Investors	3	0
115,039	5	Capital International – Global Equities	301,757	14
0	0	Capital International – Emerging Markets	30,556	1
338,390	16	Fidelity Pensions Management	285,550	13
0	0	HarbourVest	2,715	0
0	0	Henderson Global Investors	182,350	8
19,531	1	JP Morgan Fleming Asset Management	0	0
0	0	Legal and General Investment Management	539,586	25
168,680	8	Morley Fund Management	0	0
178,884	8	Prudential M&G	226,077	10
57,395	3	Schroder Investment Management	134,331	6
677,284	31	UBS Global Asset Management	297,654	14
42,363	2	Managed In-House	38,725	2
2,176,052	100		2,201,316	100

13. Additional Voluntary Contributions

The Fund offers two types of AVC arrangements.

Additional years of services may be purchased within the Local Government Pension Scheme, with the contributions being invested as a part of the Fund's assets.

In addition, the Pensions Committee appointed Equitable Life Assurance Society in 1989 and The Prudential Assurance Company in 2001 for the investment of other AVCs specifically taken out by Fund members.

These schemes, which are independently operated by Equitable Life and The Prudential were valued at £4.892 million and £0.887 million, respectively, as at 31st March 2002. (As at 31st March 2001 the Equitable Life Scheme was valued at £5.194 million and the Prudential Scheme was valued at nil. Whilst The Prudential was appointed in 2000/01 the administration arrangements had not been finalised by the year end).

14. Taxation

UK Tax

The Fund is an exempt approved fund and is not liable to income tax or capital gains tax.

The Fund is not registered separately from the Council for VAT and therefore can recover its input tax.

All investment income in the accounts has been shown gross of UK income tax and the non-recoverable element has been shown as an expense.

Overseas Tax

The Fund is subject to withholding tax in certain overseas countries. In all such cases, the investment income has been grossed up and non-recoverable tax has been shown as an expense.

15. Derivatives

A number of derivative instruments have been used by the Fund.

The Fund has used FT-SE 100 Index Futures to implement changes in asset allocation. As at 31st March 2002, the Fund was not holding any open futures contracts.

The Fund has used Forward Currency Contracts to hedge the currency exposure on overseas investments. As at 31st March 2002, the Fund held a range of positions which together showed an unrealised profit of £0.251 million. The positions showed an overall loss of £0.725 million when unwound.

16. Underwriting

The Fund accepts a number of underwriting and placing propositions. As at 31st March 2002, no commitments were outstanding.

17. Significant Holdings

As at 31st March 2002, the Fund had two holdings which represented more than 5% of the total Fund value. Both of these holdings are insurance contracts which provide access to a pool of underlying assets. These are:

- Legal and General Assurance (Pensions Management) Limited - Managed Fund. As at 31st March 2002 this was valued at £516.5 million and represented 22.3% of the total Fund value.
- Prudential Pensions Limited - Corporate Bond All Stocks Fund. As at 31st March 2002 this was valued at £179.9 million and represented 8.1% of the total Fund value.

18. Private Equity

As at 31st March 2002 the Fund had two outstanding commitments to Private Equity Investments:

- HarbourVest International Private Equity Partners IV. A total commitment of $55 million has been made with one drawdown to the value of $4.95 million having taken place. At the year end there was an outstanding commitment of $50.05 million (£35.15 million, based on the exchange rate as at 31st March 2002)
- Capital North East. A total commitment of £1.5 million has been made with one drawdown to the value of £150,000 having taken place. At the year end there was an outstanding commitment of £1.35 million.

19. Audit

The accounts are presented subject to audit.

Organisations Participating in the Fund

	Members As At 31st March 2002		
	Contributors	Deferred	Pensioners
Metropolitan District Councils			
Gateshead	7,795	1,688	4,337
Newcastle Upon Tyne	8,621	2,558	6,073
North Tyneside	5,643	1,543	3,388
South Tyneside	5,335	1,401	3,079
Sunderland	7,517	2,684	5,247
Other Scheduled Bodies			
Birtley Town Council	8	2	2
City of Sunderland College	399	53	47
Former North East Regional Airport	0	0	43
Former Tyne and Wear County Council	0	127	317
Former Tyne and Wear Residuary Body	0	6	29
Gateshead College	187	55	29
Monkwearmouth College	0	1	0
Newcastle College	329	115	86
Newcastle Education Action Zone	9	2	0
Nexus	992	408	1,428
North Tyneside College	143	30	14
Northumbria Police Authority	1,476	485	826
Northumbria Probation and After Care Service	557	127	227
South Tyneside College	287	43	58
South Tyneside Education Action Zone	2	0	0
Sunderland Education Action Zone	1	0	0
Tyne and Wear Fire and Civil Defence Authority	265	59	150
Tyne and Wear Paggenger Transport Authority	95	26	62
Tynemouth College	50	16	6
University of Northumbria At Newcastle	1,446	415	344
University of Sunderland	855	300	220
Wearside College	0	6	0
Admitted Bodies			
Age Concern Newcastle	72	11	14
Assessment and Qualification Alliance	0	4	15
Association of North East Councils	18	4	3
Benton Grange School	0	0	9
Blue Square Trading	6	0	0
Brunswick Young Peoples Project	2	0	0
Catholic Care North East	0	32	24
Disability North	28	8	2
Gateshead Law Centre	8	5	0
Gateshead Magistrates	0	10	16
Hebburn Neighbourhood Advice Centre	3	0	0
Higher Education Funding Council for England	0	2	8
Information North (Northern Regional Library System)	0	1	1
International Centre For Life Trust	13	5	2
Learning World	2	2	0
National Glass Centre	0	1	0
North East Museums Libraries and Archives Council	11	0	1
Newcastle Community Law Centre	3	1	1
Newcastle Family Service Unit	0	4	3
Newcastle Healthy City Project	5	0	0
Newcastle Magistrates	0	20	17

	Contributors	Deferred	Pensioners
Newcastle International Airport Company Limited	457	131	216
Newcastle Tenants Federation	5	3	1
Newcastle West End Partnership	0	2	0
Newcastle Youth Congress	2	1	0
Norcare	0	1	1
Norland Road Community Association	0	0	0
North East Innovation and Development Co. Limited	15	7	6
North East Regional Employers Organisation	8	1	4
North Tyneside Child Care Enterprise	3	15	1
North Tyneside City Challenge	8	2	0
North Tyneside Disability Advice Centre	0	0	1
North Tyneside Magistrates	0	8	8
Northern Arts Association	1	64	6
Northern Council For Further Education	1	15	13
Northern Counties School For The Deaf	35	13	19
Northern Informatics Application Agency	0	0	0
Northumbria Tourist Board	22	21	7
One North East	0	3	6
Ouseburn Trust	1	1	0
Park View Sports Complex	4	2	0
Passenger Transport Company	0	0	98
Port of Tyne Authority	0	0	8
Praxis Service	3	2	0
Raich Carter Sports Complex	24	0	0
Saint Mary Magdalene and Holy Jesus Charity	9	2	3
Search Project	2	0	1
Simonside Community Centre	1	0	0
South Tyneside Groundwork Trust	7	3	0
South Tyneside Magistrates	0	5	20
South Tyneside Victim Support	2	0	0
Stagecoach Travel Services (Busways)	307	207	490
Sunderland City Training and Enterprise Council	1	86	17
Sunderland Empire Theatre Trust Limited	0	9	4
Sunderland Housing Group	1,326	29	18
Sunderland Magistrates	0	8	22
Sunderland Outdoor Activities Association	0	3	0
Theatre Royal Trust Limited	51	12	14
The Hospital of St Mary the Virgin	0	0	1
The Ozanam House Probation Hostel Committee	12	8	4
Thomas Gaughan Community Centre	0	0	0
Tyne and Wear Development Company Limited	9	10	2
Tyne and Wear Development Corporation	0	38	21
Tyne and Wear Enterprise Trust Limited	21	9	9
Tyne and Wear Play Association	1	0	0
Tyne and Wear Small Business Service	53	2	14
Tyne Waste Limited	0	14	8
Tyneside Deaf Youth Project	3	0	0
Tyneside Training and Enterprise Council	0	151	26
Valley Citizen's Advice Bureau	0	2	0
Wallsend Citizens Advice Centre	3	0	0
Wallsend Peoples Centre	4	1	0
Wellfield Middle School	0	0	0
Workshops For The Adult Blind (Palatine Products)	1	19	94
Totals	**44,585**	**13,170**	**27,291**

Tyne and Wear Pension Fund

Statement of Investment Principles

Adopted - 30th September 2002

Introduction

1. The Local Government Pension Scheme Regulations require an administering authority to prepare, maintain and publish a written statement of the principles that govern their decisions about investment. This document forms that statement.

2. In the course of preparing this statement, the Pensions Committee (the Committee) has sought advice from the Fund's Actuary and Investment Advisor.

3. The Committee reviews the Statement annually, or more frequently if required.

4. The Statement is provided to the Fund's investment managers, who are required to follow the principles that it sets out and to report showing how they have done so.

Governance

5. South Tyneside Metropolitan Borough Council is the administering authority of the local government pension fund set up for the Tyne and Wear County area.

6. The Council has set up a Pensions Committee that is required to control and resolve all matters relating to the administration and investment of the Fund. The Committee has fifteen members. South Tyneside Council nominates eight members and the other four district councils within the County area nominate one member each. The trades unions nominate three members, who sit in an advisory capacity.

7. The local authority members are remunerated in accordance with each council's scheme of allowances.

8. The Council has set up a Resources and Corporate Development Scrutiny Committee to review and scrutinise the decisions and actions of the Pensions Committee.

9. A training programme is provided for members of both committees.

10. Watson Wyatt has been appointed to act as both Actuary and Investment Advisor.

11. The Committee meets quarterly to consider investment matters. It sets the investment objectives and policy, whilst responsibility for tactical asset allocation and for the selection, retention and realisation of specific investments has been delegated to external investment managers.

12. The performance of the managers is measured by independent external agencies.

13. The detailed formal monitoring of the investment of the Fund is undertaken by an Investment Panel, which is comprised of three

Committee Members, two of the Fund's Officers and the Investment Advisor. The Panel meets quarterly to consider the investment objectives and policy and each manager's performance and process. It reports to the Committee on its findings and makes recommendations on any action that is required.

14. If the Committee accepts a Panel recommendation to review and change the investment objectives or policy, or the management structure, or a manager's appointment, the Committee will require the Panel to implement that change. If a formal review of a manager's appointment is required, this will result in a tendering process, as required by law.

15. The Fund's Officers undertake the day to day monitoring of the investment of the Fund.

16. The Fund has a business plan that sets out in detail the development of the structure and processes that govern the investment of the Fund.

Investment Objectives and Policy

17. The investment objectives of the Fund are:

- To maintain securely a portfolio of assets of appropriate liquidity which will generate income and capital growth which, together with employer and employee contributions, will meet the cost of current and future benefits which the Fund provides, as set out in the statutory documentation.
- To minimise the long term costs of the Fund by maximising the return on the assets, whilst having regard to the objective stated above.
- To comply with the regulations relating to the investment of local government pension funds.

18. In order to assist in setting the Fund's strategic investment policy, an asset liability modelling study was carried out. This study examined the Fund's financial position, the profile of its membership, the nature of its liabilities and included an analysis of the expected ranges of outcomes from differing investment policies. The study was initially undertaken in 2000, but then updated in 2001 to reflect information on the liabilities derived from the actuarial valuation undertaken as at 31st March 2001. The projected investment returns that were used in the study are shown in Appendix A.

19. Having considered the outcome of the study, the Committee concluded that a diversified portfolio, of which about 65% is invested in UK and overseas equities and about 35% is invested in bonds and property, currently represents a suitable strategic asset allocation benchmark for the Fund. The degree and nature of risks attaching to such a portfolio are considered by the Committee to be appropriate, when taken in conjunction with the expected returns, for the Fund.

20. Appendix B sets out the detail of the strategic benchmark.

21. The strategic benchmark was implemented from 1st July 2002.

22. The Committee will continue to monitor the suitability of this policy in the light of the Fund's developing liabilities and finances.

Investment Management Structure

23. The Committee considers that the Fund must have an investment management structure that provides exposure to a suitably diversified, but complementary, range of investment styles and processes.

24. It is the view of the Committee that the strategic benchmark is best implemented by investing the entire Fund on a specialist basis, using passive asset allocation and a combination of active and passive stock selection.

25. The structure includes discretionary mandates for the active management of UK equities, Pan European equities, Global equities, Pacific equities, Emerging Market equities, Global bonds and Corporate bonds.

26. Following consideration of the efficiency, liquidity and level of transaction costs likely to prevail within each market, the Committee determined that about 25% of the Fund should be managed on a passive basis. The passive mandate includes a proportion of the total allocation to UK equities, US equities and UK Government bonds.

27. It is intended that up to 5% of the Fund is to be invested in Private Equity. This position will be built up over a period of years, largely by investment in funds of funds. The allocation will be top-sliced from the allocation to quoted equities.

28. The Fund's Officers monitor the overall allocation of the Fund's assets, relative to the strategic benchmark, with assistance from the passive manager. In the light of this monitoring, the actual asset allocation is maintained within agreed margins around the strategic benchmark by the direction of cash flow or the reallocation of assets between portfolios, as appropriate.

29. Independent custodians have been appointed to take responsibility for the safe keeping of the assets within each of the Fund's stock market portfolios. The Fund's Officers monitor the operation of the custodians.

30. The Property portfolio is managed on an advisory basis. The manager is also responsible for advising on the tactical allocation to property, for which purpose the benchmark allocation is set at 7.5% of the Fund.

31. The Committee's expectations in respect of returns from the Fund's investments are expressed through achievable and prudent objectives and restrictions that have been set for each mandate. The objectives and restrictions have been discussed and agreed with each manager with the aims of ensuring a prudent approach to investment and of allowing each manager to implement their natural investment style and process. The use of any financial instruments is not prohibited, except where such prohibition is required by legislation or it has been agreed with a manager that its use is inappropriate.

32. Appendix C sets out details of the individual mandates.

33. The managers are remunerated by way of ad valorem fees. Performance fees have received consideration but none have been adopted because the fee structures were not found to be satisfactory.

34. The Investment Advisor is remunerated by reference to the time and resources expended in that role.

35. The managers are permitted to use soft commission arrangements within their broking transactions where the Committee believes this practice to be a satisfactory approach for the manager to access resources in the most cost efficient way to the Fund.

Diversification

36. The strategic asset allocation benchmark and the investment objectives and restrictions placed upon the managers are designed to ensure that the Fund's investments are adequately diversified.

37. Within each asset category in each portfolio, the manager concerned is responsible for appropriate diversification.

38. The restrictions ensure that, at a stock selection level, the Fund avoids undue concentration.

Suitability

39. The Committee has taken advice from the Actuary and Investment Advisor to ensure that the strategic asset allocation benchmark is suitable for the Fund, given its financial position, statutory status and liability profile.

40. Within each of the Fund's portfolios, and within each asset category in those portfolios, the manager concerned is responsible for the suitability of individual investments.

Realisation of Assets

41. The Fund maintains sufficient investment in liquid or readily realisable assets to meet the payment of benefits, together with a margin for unexpected cashflow requirements so that, whenever possible, the realisation of assets will not disrupt the overall investment policy. When the Committee requires assets to be realised out of a portfolio in order to meet cashflow requirements or to reinvest the proceeds elsewhere, the realisation of individual holdings is at the discretion of the manager of the portfolio.

Risk

42. The Committee recognises that there are a number of risks involved in the investment of the assets. The policy is to minimise these risks as far as possible, consistent with earning a satisfactory return on investments. In particular:

- Solvency risk and mismatching risk is controlled through the asset allocation strategy and through ongoing triennial actuarial valuations.
- Liquidity risk is controlled by estimating the annual net benefit outgo or inflow and liasing with the managers to ensure that sufficient cash balances are available.
- Manager risk is controlled through the investment objectives and restrictions set out in each manager's agreement and through the ongoing monitoring of the managers.
- Custodian risk is controlled through the restrictions set out in each custodian's agreement and through the ongoing monitoring of the custodial arrangements.
- Position, currency and political risks are controlled through the approach to diversification.
- Counterparty risk is controlled through the restrictions followed by the managers with respect to the trading of securities and cash management.

Socially Responsible Investment

43. Responsibility for the selection, retention and realisation of investments is delegated to the managers.

44. The Committee has reviewed and will continue to review from time to time the policies operated by each of the Fund's managers in respect of social, environmental or ethical considerations. Having done so, the policy of the Committee is that the extent to which such considerations are taken into account in these decisions is at the discretion of each manager. However, active managers must take such considerations into account where they may have a financial impact on the portfolio. The passive manager is not required to take account of such considerations in the selection, retention and realisation of investments.

45. Each manager is urged to pursue a policy of engagement with companies and to take account of such considerations in its corporate governance and voting policy.

46. Each manager must continue to develop its policy and provide a quarterly report that sets out how it has been implemented.

Rights Attaching to Investments

47. Responsibility for the exercising of rights, including voting rights, attaching to investments is delegated to the managers.

Corporate Governance and Voting

48. Each manager is required to prepare and implement a policy on corporate governance and voting. The policy towards U.K. quoted companies should take account of the principles contained in the Combined Code and of the guidance offered by relevant organisations, whilst the policy towards companies outside the UK should take account of the practices of the home nation.

49. Voting rights must be exercised in a manner that establishes a consistent approach to both routine and exceptional issues in order that company directors fully understand the manager's views and intentions.

50. Whilst it has not been made compulsory for the managers to vote, they are strongly urged to do so.

51. Each manager must continue to develop its policy and provide a quarterly report that sets out how it has been implemented.

Additional Voluntary Contributions

52. The Fund provides a facility for members to pay additional voluntary contributions (AVCs) to enhance their benefits. Members have a choice between buying added years of service or accumulating their AVCs to purchase benefits on a money purchase basis. Investment of money purchase AVCs is undertaken through the Prudential Assurance Company Limited and Equitable Life Assurance Society. The Committee's intention is to offer a range of funds that are intended to provide a suitable long-term return for members, consistent with the degree of risk accepted. The Fund's Officers monitor the returns obtained on members' AVC investment and the Committee reviews annually the suitability of the AVC providers used.

Compliance with Principles of Investment Practice

53. The Fund complies with the Principles of Investment Practice, as set out in the document called CIPFA Pensions Panel Principles or Investment Decision Making in the Local Government Pension Scheme, except in the areas stated below:

- The provision of a handbook to each Committee member containing terms of reference, standing orders and operational procedures (Principle 1).
- Contracts for actuarial and investment advice should be opened to separate competition (Principle 4).
- Monitoring of transaction related costs (Principle 5).
- The formal assessment of decisions taken by the Committee and its advisors (Principle 8).

54. Further consideration is required prior to compliance being achieved in these four areas.

55. Consideration is being given to a number of initiatives with the aim of increasing compliance by 31st March 2003, when the position will be reviewed.

Appendix A

Asset Liability Study

Projected Investment Returns

The asset liability modelling study involves ten year projections of the Fund's liabilities and of returns from the various asset classes, over a large number of scenarios. Implicit within that process is a distribution of expected returns for each asset class over the ten year period. The table below shows the median real returns (i.e. returns in excess of price inflation) from the distributions in respect of the main asset classes, as used in the 2001 update of the study.

Asset class	10 year median real return % pa
Global (ex UK) Equities (unhedged)	5.6
UK Equities	5.2
Property	4.5
Private Equity	5.4
AA Sterling Long-Dated Corporate Bonds	3.1
Long-Dated UK Gilts	2.2
UK Index-Linked Gilts	2.3
Foreign Bonds (unhedged)	3.0
Cash	2.0

However, the results of the asset liability modelling study reflect not only these median returns, but also more complex factors such as:

- the volatility of returns from each asset class;
- the degree to which returns from one asset class are linked to returns from other classes;
- the relationship between movements in assets and movements in liabilities.

The returns shown above were those projected from 31 March 2001 and hence would not necessarily apply at any subsequent date.

Appendix B

Strategic Benchmark

Asset Class	Allocation %	Index
UK Equities	**30.00**	FTSE All Share
Overseas Equities	**35.00**	
- US	9.75	FTSE All World US
- Europe ex UK	12.25	FTSE World Europe ex UK
- Japan	6.50	FTSE All World Japan
- Other Far East	3.25	MSCI All Country Pacific Free ex Japan inc Malaysia
- Emerging Markets	3.25	MSCI Emerging Markets Free
Fixed Interest	**27.50**	
- UK Gilts	8.75	FTSE-A British Govt All Stocks
- UK Index- Linked	5.00	FTSE-A British Govt Over 5 Year IL
- Sterling Non Government	11.00	ML Sterling Non Gilt All Stocks
- Overseas	2.75	JPM Global (non UK) Traded Bond Index, hedged into Sterling
Property	**7.50**	CAPS Property

Note

Up to 5% of the Fund is to be invested in Private Equity. This position will be built up over a period of years and will be top-sliced from the allocation to quoted equities.

Appendix C

Management Structure

Manager	Mandate	Proportion of Fund %	Mandate
Fidelity	UK Equities	13	To outperform the FTSE All Share Index by + 1.5% p.a. over 3 year rolling periods with the return being no more than 4% below the Index in any one year.
UBS	Pan European Equities	13	To outperform the FTSE Europe (including UK) Index – Developed Series by 2% p.a. over 3 year rolling periods with the return being no more than 5% below the Index in any one year.
Capital International	Global Equities	13	To outperform the FTSE All World Index by 1.5% pa over 3 year rolling periods with the return being no more than 5% below the Index in any one year.
Capital International	Emerging Market Equities	3	To outperform the FTSE Emerging Markets Free Index
Schroders	Japanese Equities	5	To outperform the FTSE All World Japan Index by 2% pa over 3 year rolling periods with the return being no more than 4% below the Index in any one year.
Schroders	Pacific ex Japan Equities	3	To outperform the MSCI All Countries Pacific Free ex Japan Index by 2% over 3 year rolling periods with the return being no more than 5% below the Index in any one year.
Various	Private Equity	Up to 5% of fund, to be topsliced from the equity allocation	Notionally, 5% above the returns on quoted equity.

Manager	Mandate	Proportion of Fund %	Mandate
Legal and General	UK Equities	11	To match the return on the FTSE All Share Index
Legal and General	US Equities	3	To track the total return of the FTSE World North America Index within expected tolerances of +/-0.5% in two years out of three.
Legal and General	UK Index Linked	4	To match the return on the FTSE – A Over Five Years Index-Linked Index
Legal and General	AAA Fixed Interest	4	To match the return on the Merrill Lynch AAA All Stocks Index
Prudential M&G	Corporate Bonds	11	To outperform a composite benchmark by 0.75% pa over three year rolling periods with the return being no more than 2% below the Index in any one year. The benchmark is: 80% Merrill Lynch Sterling Non Gilt All Stocks 15% FTSE - A British Government All Stocks 5% FTSE - A British Government Over 5 Year Index-Linked

Manager	Mandate	Proportion of Fund %	Mandate
Henderson	Government Bonds	9	To outperform a composite benchmark by 0.75% pa over three year rolling periods with the return being no more than 2% below the Index in any one year. The benchmark is: 37.5% FTSE – A British Government All Stocks 7.5% FTSE – A Over Five Years Index-Linked 25% Merrill Lynch Sterling Non Gilt All Stocks 30% JP Morgan Global (Non UK) Traded Bond Index, hedged into Sterling.
Aberdeen Property Investors	Property	8	To outperform the IPD All Funds Universe by 0.5% pa over 3 year rolling periods.

Policy on Socially Responsible Investment, The Exercise of Rights And Corporate Governance

Approved by Pensions Committee 31st May 2002

Introduction

1. This document sets out the Fund's policy on Socially Responsible Investment, the Exercise of Rights and Corporate Governance.

2. The Pensions Committee reviews the policy annually, or more frequently if required.

3. The Committee provides copies of this document to the Fund's investment managers, who are required to follow the principles that it sets out and to report showing how they have done so.

Development of a Manager's Policy

4. Each manager must prepare and implement a policy on Socially Responsible Investment, corporate governance and the principles that govern the way in which voting rights are exercised.

5. If a manager's policy is inconsistent with the requirements set out in this document, the issues will be discussed with the manager and an approach will be agreed.

6. Each manager must continue to develop its policy and report change as soon as practicable.

Socially Responsible Investment

7. Responsibility for the selection, retention and realisation of investments is delegated to the managers, who are required to act within specified guidelines and restrictions.

8. The extent to which social, environmental or ethical considerations are taken into account in this decision is at the discretion of each manager.

9. However, active managers must take such considerations into account where they may have a financial impact on a portfolio.

10. Part of the Fund's assets are invested on a passive basis. The passive manager is not required to take account of such considerations in the selection, retention and realisation of investments.

11. Each manager is urged to pursue a policy of engagement with companies and to take account of such considerations in its corporate governance and voting policy.

Rights Attaching to Investments

12. Responsibility for the exercising of rights, including voting rights, attaching to investments is delegated to the managers.

Corporate Governance

13. The policy towards UK quoted companies should take account of the principles contained in the Combined Code and of the guidance offered by relevant organisations.

14. The policy towards companies outside the UK should take account of the practices of the home nation.

15. The policy towards unquoted companies should be consistent with the approach adopted for quoted companies, to the extent that this is practicable.

Voting Rights

16. Voting rights should be exercised in an informed manner. Therefore, in general, the managers are most appropriately placed to undertake this task.

17. Voting rights are regarded as an asset that needs managing with the same duty of care as any other asset. Exercising the rights attached to shares is essential to protect the interests of the organisations participating in the Fund and the beneficiaries of the Fund.

18. Whilst it has not been made compulsory for the managers to vote, they are strongly urged to do so.

19. Voting rights must be exercised in a manner that establishes a consistent approach to both routine and exceptional issues in order that company directors fully understand the manager's views and intentions.

20. Whilst the responsibility is delegated to each manager to exercise voting rights in accordance with its own policy, the Committee retains the right to direct each manager in respect of any issue.

21. Prior to voting, each manager is required to use reasonable endeavours to consider whether, in their opinion, any issue could become controversial for the Fund or the organisations participating in the Fund. If this is the case, the issue should be referred to the Fund's officers for discussion and possibly direction. It is considered that this will happen infrequently. Whilst each manager should exercise their own discretion as to what may fall into this category, examples may be:

- Where the manager intends to vote against directors on a major issue.
- Matters affecting the local economy.
- Political donations.

Review and Reporting Arrangements

22. Each manager's policy will be reviewed and its impact monitored on a regular basis.

23. Policy changes must be reported as soon as practicable.

24. Each manager must provide a quarterly report that sets out how its policies have been implemented.

25. The quarterly report must include:

- The proportion and numbers of votes which were cast.
- A summary and explanation of instances where:
  - Voting rights were exercised in a manner that was inconsistent with the normal policy
  - Voting rights were exercised against management
  - The manager abstained from voting
  - Voting rights were not exercised.

CONTACTS

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Notes