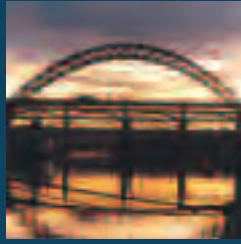


# Tyne and Wear Pension Fund

Administered by South Tyneside Council



## Report and Accounts 2004/05



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“The role of Pensions Committee will be to control and resolve all matters relating to the administration of the Tyne and Wear Pension Fund and the management and investment of the assets of the Fund”.



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

## Committee Members

<b>South Tyneside Council</b>	Councillor S. Stratford (Chair) Councillor W. Lynch (Vice Chair) Councillor E. Battye Councillor G.R.W. Elsom Councillor E.M. Gibson Councillor J.N. McKie Councillor A. Meeks Councillor M.M. Robinson
<b>Gateshead Council</b>	Councillor J.I. Mearns (substitute – Councillor K. Childs)
<b>Newcastle City Council</b>	Councillor D. Slesenger (substitute – Councillor B. Renton)
<b>North Tyneside Council</b>	Councillor C.B. Francis (substitute – Councillor N. Clothier)
<b>City of Sunderland Council</b>	Councillor J. Heron (substitute – Councillor P. Young)
<b>Trades Union Representatives</b>	G. Clements – UNISON W. Flynn – UCATT S. Forster – UNISON
<b>Employer's Representatives</b>	J. Fenwick – National Probation Service - Northumbria D. Chesser – Northumbria University D. Scott – Stagecoach Travel Services

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## Investment Managers

<b>Indexation</b>	Legal and General Investment Management
<b>Global Equities</b>	Capital International
<b>Emerging Market Equities</b>	Capital International
<b>Pan European Equities</b>	UBS Global Asset Management
<b>UK Equities</b>	Fidelity Pensions Management
<b>Far East Equities</b>	Schroder Investment Management
<b>Corporate Bonds</b>	Prudential M&G
<b>Global Government Bonds</b>	Henderson Global Investors
<b>Property Manager</b>	Arlington Property Investors
<b>AVC Providers</b>	The Prudential Assurance Company Equitable Life Assurance Society

## Advisors

<b>Actuary</b>	Hewitt Bacon and Woodrow Limited
<b>Investment Advisor</b>	Hymans Robertson Consultants and Actuaries

## Officers

<b>Executive Director Resources</b>	J. Alderson
<b>Head of Pensions</b>	S. Moore
<b>Head of Corporate Governance</b>	B.T. Scott
<b>Pensions Manager</b>	D. Smith
<b>Investment Manager</b>	I. Bainbridge

# Review of the Year

## We are pleased to present the 2004/05 Annual Report and Accounts for the Tyne and Wear Pension Fund.

During the year, we carried out a triennial valuation based on the Fund's position as at 31st March 2004. This has shown that the funding level has fallen to 64%, which is a decrease of 18% from the funding level of 82% calculated at the 2001 valuation. The fall is largely attributable to the worldwide bear market in equities that took place between 2000 and 2003. This led to investment returns being below the level assumed in the 2001 valuation, although this was alleviated in part by the Fund's performance being stronger than the peer group return. Movements in interest rates also contributed to the fall.

This fall in the funding level was expected because the Fund had undertaken a programme of annual interim valuations. The interim valuation carried out as at 30th September 2003 calculated a funding level of 63%.

It has been necessary to increase employers' contributions from 1st April 2005 in order to address the fall in the funding level. The Fund has used a number of measures to assist employers to manage this, the most significant being an increase in the deficit recovery period for employers with a suitably strong covenant.

The changes resulting from Phase II of the Stocktake of the Scheme were taken into account in this valuation and led to a reduction of about 30% in future service rates. This is because the changes were law as at 1st April 2005. On 13th July 2005, the Office of the Deputy Prime Minister (ODPM) announced that the changes would be revoked with retrospective effect from 1st April 2005. At the time of writing, we are considering the impact of this

revocation on the solvency of the Fund.

The Fund's strategic investment policy is derived from an asset liability study that was first undertaken in 2000. This study indicated that a diversified portfolio invested 30% in UK Equities, 35% in Overseas Equities, 27.5% in Bonds and 7.5% in Property, represented a suitable strategic benchmark for the Fund. Up to 5% of the Fund is to be invested in Private Equity, with this being sourced out of the allocation to Quoted Equity.

The outcome of this initial study was tested against updated investment data and rolled forward liability data in each year to 2003/04 and was found to remain appropriate. This ongoing exercise has ensured that the Fund has been properly invested in relation to its liabilities and to opportunities in investment markets.

The benchmark has been subject to a fundamental review during 2004/05. This was undertaken by the Fund's Investment Advisor, Hymans Robertson, and has used the liability data from the 2004 valuation that was prepared by our Actuary, Hewitt Bacon and Woodrow.

**This review has determined that the optimal investment strategy for the Fund, going forward, is 27.5% in UK Equities, 40% in Overseas Equities, 22.5% in Bonds and 10% in Property. This represents increases of 2.5% in both Equities and Property, funded by a reduction in the Bonds exposure of 5%.**

The changes to the benchmark are being implemented in 2005/06 through the existing investment management structure.

The allocation to Private Equity remains unchanged at 5%. In order to assist with achieving this allocation, the Fund has decided to commit to funds managed by Pantheon, Lexington and Capital International to run alongside our existing programme of investment with HarbourVest.

With regard to investment performance, rising Equity markets led to pension funds being able to deliver positive returns for the second year in succession. This period of recovery followed three years of negative returns during which Equity values declined significantly from the high point attained in early 2000.

**The Fund's return for the year was 10.9%, which is in line with our benchmark.**

In order to avoid taking too short term a view of investment performance, we focus more on the return achieved over five year periods. The Fund's annual return over the last five years has been 2.0% per annum, with the decline in Equity markets from March 2000 to March 2003 being the main reason for this low return.

Whilst this return is disappointing in absolute terms and lags both inflation and the increase in average earnings over the period, it is above the benchmark return of 0.5% per annum.

**The Fund has continued to work to improve the service we offer to employers and members.**

We continue to offer training courses to employers. Pensions matters and working procedures are discussed at our annual general meeting and at regular liaison meetings.

Since 1999 the Fund has produced annual benefit statements for its current contributors. In 2004 the Fund worked in partnership with the Department of Work and Pensions on a pilot scheme for combined benefit statements. This pilot was targeted on 10% of our current contributors, who received information on their State Pension entitlement in addition to the statement on Scheme benefits. The pilot was successful and we are working to provide all current contributors with a combined benefit statement in 2005.

Statements were introduced for deferred members on request in 2003. From 2004, we have produced statements for the majority of our deferred members.

The Fund is committed to continually improving its services to members and employers. To assist with this process, we seek their views on the service we offer. In 2004/05, we issued surveys to our current contributors and employers. We were pleased to see that 98% of our current contributors who responded stated they were satisfied with the service we provide, as did 92% of the employers who responded to their survey.



**Councillor Shirley Stratford  
Chair of Pensions Committee**



**Julie Alderson  
Executive Director Resources**

# Statement of Responsibilities

## The Council is required:

- To make arrangements for the proper administration of the financial affairs of the Tyne and Wear Pension Fund and to ensure that one of its Officers has the responsibility for the administration of those affairs. For Tyne and Wear Pension Fund, that Officer is the Executive Director Resources.
- To manage the affairs to secure economic, efficient and effective use of resources and safeguard its assets.

## The responsibilities of the Executive Director Resources

*The Executive Director Resources is responsible for the preparation of the Pension Fund's statement of accounts which, in terms of the CIPFA/LASAAC Code of Practice on*

*Local Authority Accounting in Great Britain ('the Code'), is required to present fairly the financial position of the Pension Fund at the accounting date and its income and expenditure for the year ended 31st March 2005.*

## In preparing this Statement of Accounts, the Executive Director Resources has:

- Selected suitable accounting policies and then applied them consistently.
- Made judgements and estimates that were reasonable and prudent.
- Complied with the Code.


## The Executive Director Resources has also:

- Kept proper accounting records which were up to date.
- Taken reasonable steps for the prevention and detection of fraud and other irregularities.

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## Chief Finance Officer's Certificate

I hereby certify that the Statement of Accounts for the year ended 31st March 2005 set out in the following pages presents fairly the financial position of the Tyne and Wear Pension Fund at 31st March 2005 and its income and expenditure for the year ended 31st March 2005.


Signed:.....

Date: 12th September 2005.....

Julie Alderson, Executive Director Resources

## Chair of Pensions Committee's Certificate

I can confirm that these Accounts were approved by the Pensions Committee at its meeting held on 12th September 2005.

Signed:.....

Date: 12th September 2005.....

Councillor Shirley Stratford – Chair of Pensions Committee



# Governance Arrangements

**South Tyneside Council is the administering authority of 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, whose role is set out in the Council's Constitution as follows:

"The role of Pensions Committee will be to control and resolve all matters relating to the administration of the Tyne and Wear Pension Fund and the management and investment of the assets of the Fund.

The responsibilities to be discharged by the Committee include:

- Ensuring that the Fund complies with the Local Government Pension Scheme Regulations 1997, the Local Government (Management and Investment of Funds) Regulations 1998 and all other legislation governing the administration of the Fund.
- Ensuring the Fund is valued as required and receiving and considering reports on each valuation.
- Ensuring appropriate arrangements for the administration of benefits are in place.
- Setting the admissions policy.
- Setting the strategy for communicating with Scheme Employers and Members.
- Ensuring appropriate AVC arrangements are in place.
- Setting the investment objectives and policy and the strategic asset allocation.

- Appointing, dismissing and assessing the performance of Investment Managers and Custodians.
- Preparing, approving and reviewing the Statement of Investment Principles."

The Committee has eighteen 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 representatives and, since November 2004, we also have three representatives of the employers sitting on the Committee.

The Committee meets quarterly to consider pension matters. Additional meetings are called should an aspect of the Fund require an in depth review.

Annual meetings are held for the employers and the trades unions. The agenda for these meetings covers the actuarial position, investment performance and the benefits structure, and includes presentations by the Actuary and the Investment Advisor.

The Committee has an Investment Panel to provide a greater focus on, and scrutiny over, the performance and strategy of investment managers. The Panel consists of three members of the Pensions Committee, the Investment Advisor, 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.

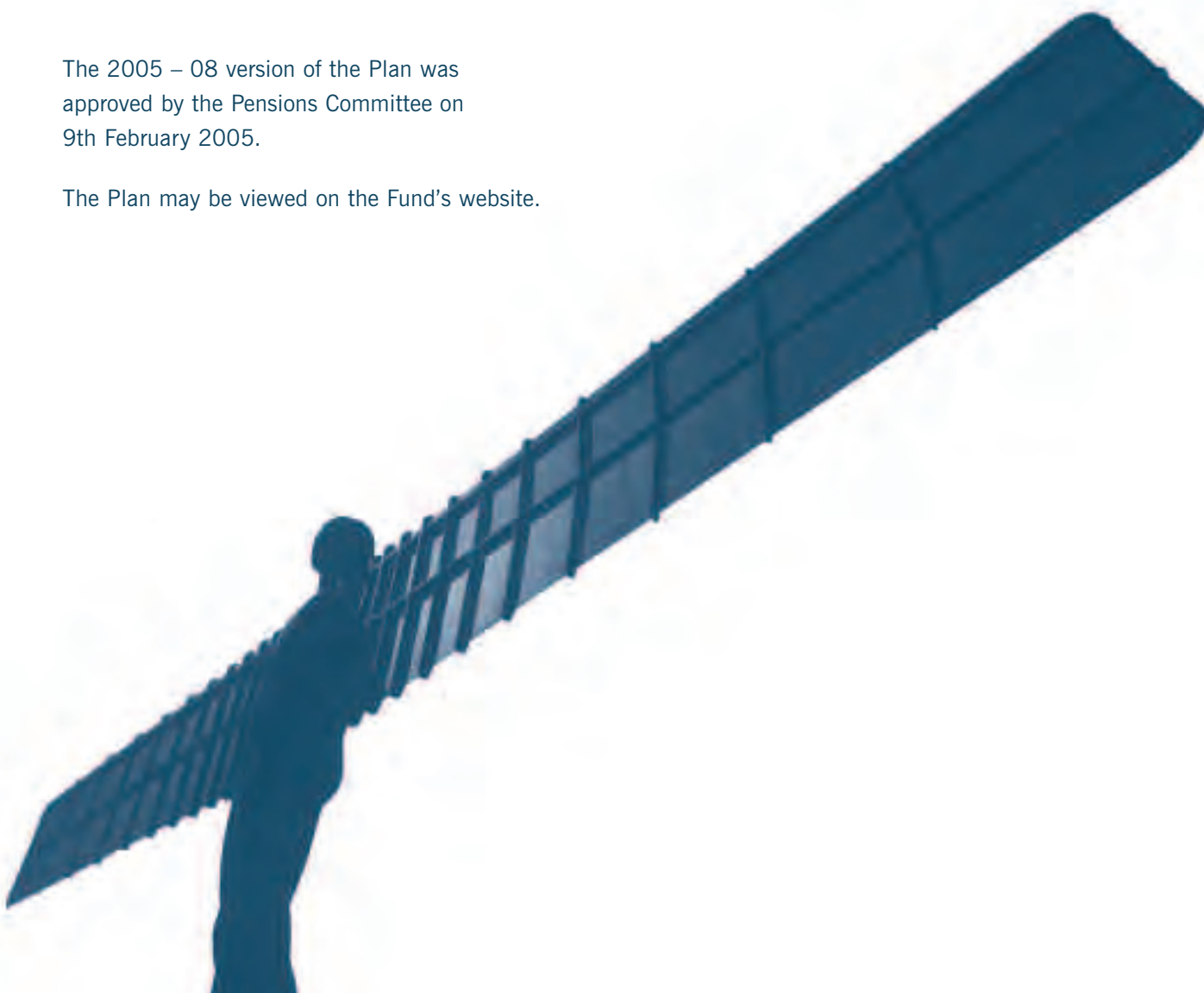
Further information on the governance structure may be viewed on the Fund's website for which the address is [www.twpf.info](http://www.twpf.info)

## Service Plan and Vision Statement

The vision and aims of the Fund are set out in our Service Plan. This is a three year rolling plan that is reviewed annually. It sets out the actions that we must concentrate on in order to achieve our vision.

The 2005 – 08 version of the Plan was approved by the Pensions Committee on 9th February 2005.

The Plan may be viewed on the Fund's website.



## 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
- we are consistently achieving our service standards
- we are recognised as being amongst the leading UK pension funds.

# The Legal Framework of the Scheme

## Introduction

**The framework of the Scheme is contained in Regulations that are made by the ODPM. These Regulations apply nationally to all local authorities in England and Wales.**

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 different types of investment.

The Local Government Pension Scheme Regulations 1997, as amended, set out the rates of contribution and the method of calculation of benefits.

These Regulations introduced a common contribution rate of 6% for all members. Manual workers who were members of the Scheme prior to 1st April 1998 have retained the right to pay 5% for as long as they remain in the Scheme, in continuous employment and in the same capacity.

The Scheme provides an extensive range of benefits for members and their dependents, 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.**

## The Stocktake

In July 2001, Ministers authorised a review, or a "Stocktake", of the Scheme to ensure that it is operating effectively and efficiently and that it continues to provide value for money.

A number of discussion papers have been published by the ODPM inviting comment on possible changes to the Scheme. The Local Government Pension Committee acts as the primary respondent for local government employers.

The Fund has submitted its own comments on all proposals. We have kept employers advised of progress and encouraged them to submit their own views. We have also hosted meetings between employers and the ODPM to consider the possible changes.

Phase I of the Stocktake became effective from 1st April 2004 and introduced a number of changes, most of which were relatively minor in nature and were comprised of technical changes to the Regulations. The more significant changes are:

- A requirement for administering authorities to produce a Funding Strategy Statement was introduced.
- The minimum membership period giving rise to entitlement of benefits was reduced from two years to three months.
- Tighter time scales for combining different periods of membership were brought in. On rejoining the Scheme, members have twelve months to combine any previous periods of membership, but with discretion for their employer to extend this period.
- A requirement was introduced for annual benefit statements to be provided to all active, deferred and pension credit members. The Fund was already compliant with this provision.

- The Internal Dispute Resolution procedure was changed to allow for disputes to be dealt with at a more appropriate level by filtering out easily resolved complaints and misunderstandings at an early stage. The latter stages of the process are now reserved for more difficult and contentious cases.

Phase II introduced measures that sought to contribute towards stabilising the cost of the existing Scheme. These measures are contained in the Local Government Pension Scheme (Amendment) (No. 2) Regulations 2004, which took effect from 1st April 2005. These Regulations:

- Removed the Rule of 85 voluntary early retirement provision, whereby if a members age and length of membership (in full years) add up to 85 or more, he or she could elect to retire early with their employers consent before age 65 without any reduction to their benefits.
- Increased the minimum retirement age from 50 to 55 for early retirement other than on the grounds of ill health.

Limited protection in respect of both changes was included for employees close to retirement.

The unions balloted their members over these changes. In the light of strong support for industrial action, the Deputy Prime Minister issued a statement on 18th March 2005 that set out his intention to revoke the changes and to establish a committee comprised of key stakeholders to consider and negotiate the long-term future of the Scheme.

A consultation exercise took place on the proposed revocation. We advised employers of this process and encouraged them to submit their views to the ODPM.

On 13th July 2005, the ODPM announced that the changes would be revoked with retrospective effect from 1st April 2005. At the time of writing, we are considering the impact of this revocation on the solvency of the Fund.

### The Green Paper

After having prepared the Phase II changes, but prior to their revocation, the ODPM had proceeded to Phase III of the Stocktake.

The Phase III proposals set out a far reaching review, with an intention to develop a revised Scheme that will be sustainable and affordable over the long term and will meet the continuing needs of employers, Scheme members and tax payers.

These proposals are set out in a Green Paper entitled “Facing the Future – Principles and Propositions for an Affordable and Sustainable Local Government Pension Scheme in England and Wales”.

The consultation period ended on 31st March 2005. The ODPM has stated that the responses are being carefully considered and taken into account as part of the further development work for a new look Scheme.

# Additional Voluntary Contributions

## Introduction

Whilst the 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, an AVC plan can also be used to provide extra life assurance.

## The Prudential

The Fund has an AVC plan arranged with The Prudential that offers a comprehensive range of funds, including with-profits, unit-linked and deposit funds. The unit-linked fund includes a lifestyle option.

We carry out an annual review of AVC provision. The 2004/05 review, which was carried out with the assistance of Hewitt Bacon and Woodrow, concluded that The Prudential should remain as the sole provider. This review has led to the closure of two higher risk funds and the removal of with - profits as a default option. We undertook a bulk transfer exercise on behalf of members investing in the discontinued funds, through which investments were transferred to alternative, more appropriate funds. The transfers took place between April and June 2005. All members affected were notified of the changes.

## Equitable Life

With the exception of existing life cover policies, the Fund has closed its AVC plan with Equitable Life to new members and transfers.

Acting in the light of advice from its legal and financial advisors, the Fund has conducted a bulk transfer exercise. This involved the transfer of the majority of members' Equitable Life AVC funds to comparable funds with The Prudential.

A number of members who have with - profits investments still remain with Equitable Life. This is because it is not believed to be in the individual member's best interest to transfer as the withdrawal penalty applied on transfer may not be made up by future investment returns.

**The Fund will continue to monitor the position and keep members informed.**



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



# Employers' Contributions and the Valuation Process

## Introduction

The Regulations set out the benefits that are paid under the Scheme. These benefits are paid for by employees' contributions, which are set by the Regulations, investment income and employers' contributions. The employers' contributions are adjusted in triennial valuations to ensure that the Fund will have sufficient assets to cover liabilities.

## Funding Levels

The funding position has been deteriorating for a number of years. The Fund has been in deficit since the early nineties and it is important to understand the background to this position.

The 1989 valuation revealed a funding level of 118%, with this surplus being attributable to actual investment returns having greatly exceeded expected returns. This overfunded position led to the scheduled employers agreeing to take a contributions holiday. This eroded the surplus, so that the funding level at the 1992 valuation fell to 98%. The contributions holiday was ended and an employers' contribution for the scheduled employers was gradually phased back in.

The 1995 and 1998 valuations both identified funding levels of 87%. The 1998 result was adversely affected by the removal of the tax credit that was attached to UK equity dividends, which took effect from the July 1997 budget.

The contributions paid by employers from 2002/03 to 2004/05 were set by the 2001 valuation. This valuation revealed a deterioration in the funding level from 87% to 82%, which was attributable to:

- Increasing longevity.
- Employer specific liability factors such as pay awards, restructuring, ill health retirements and early retirements.
- The investment returns in the inter valuation period being below the levels assumed in the 1998 valuation, although this was alleviated in part by the Fund's performance being strong relative to its peer group.

The worldwide bear market in Equities between 2000 and 2003 has led to a further and significant fall in the funding level. The 2004 valuation was carried out during 2004/05, based on the Fund's position as at 31st March 2004. This has shown that the funding level has fallen to 64%. This is a fall of 18% from the funding level calculated at the 2001 valuation. The fall is largely attributable to investment returns being below the level assumed in the 2001 valuation although, again, it was alleviated in part by the Fund's performance being stronger than the peer group return. Movements in interest rates also contributed to the fall.

This fall in the funding level was expected because the Fund has undertaken a programme of annual interim valuations that are carried out in the years between the triennial valuations. The interim valuation carried out as at 30th September 2003 calculated a funding level of 63%.

## Employers' Contributions

The employers' contributions that resulted from the 2004 valuation were implemented from 1st April 2005.

The average future service contribution rate is 240% of employees' contributions, whilst the contribution to meet the past service deficiency is 105%. The total rate of contribution is 345%, an increase of 30% over the rate of 315% that was set by the 2001 valuation.

## Valuation Strategy

The strategy for the 2004 valuation is set out in the Funding Strategy Statement and in the valuation report that is produced by the Actuary. Both documents may be viewed on the Fund's website.

The requirement to prepare a Funding Strategy Statement was introduced in 2004/05. It is the responsibility of each administering authority to prepare, publish and maintain the Statement, having regard to guidance and to the Statement of Investment Principles (SIP). The Fund consulted employers and considered their views in the formulation of the strategy.



The Fund has deployed a number of measures to assist employers to manage the increase in contributions, the most significant being an increase in the deficit recovery period for employers with a suitably strong covenant.

A deficit recovery period of 13 years, equivalent to the average future working lifetime of current contributors, was generally used at the 2001 valuation. It was accepted across the Scheme that longer periods had to be used at the 2004 valuation if increases in employer contributions were to be held at manageable levels. This Fund has used this approach selectively. It is an increased source of risk to the Fund and to individual employers because:

- Some employers are directly guaranteeing the deficit of admission bodies and transferee admission bodies.
- If an employer without a guarantee closes in circumstances where they could not pay the contributions due, then all employers in the Fund would be required to pay revised contributions to meet the shortfall.

On the other hand, not extending a recovery period for an employer with a poor covenant could impose an additional financial pressure that might, in extreme cases and for non statutory bodies, lead to a wind up. This could lead to a loss of the service provided by that employer.

Information supplied by employers in response to the Fund's Annual Employer Survey, last undertaken in 2004, was taken into account in setting recovery periods. In addition, all employers were asked for their views on recovery periods as part of the consultation exercise on the draft Funding Strategy Statement. Additional consultation took place with the five district councils because if an employer without a guarantee closes in circumstances where they could not pay the contributions due, a significant proportion of the shortfall would fall on the councils because they comprise such a large part of the Fund. In addition, they act as guarantors to a large number of other employers.

Having taken all views into account, deficit recovery periods have been set within the range of 25 years, for employers with the strongest covenant to average future working lifetime of active members, or an appropriate proxy for that period, for employers with a weak covenant.

For most contractors, this decision was also subject to a maximum of the remaining contract period from 1st April 2005.

Other measures were used to assist with managing the increase in contributions:

- A smoothing adjustment has been made to the market value of the assets. This takes account of asset values over the last three years and slightly increases the funding level.
- The use of up to three annual steps in the past service deficiency payments has been offered to employers. This is to assist with managing the impact of cost changes on employers.
- The Fund's policy has been to group some smaller employers for the purpose of setting contribution rates. This serves to protect such employers from the risk of high volatility of contribution rates. Following a careful consideration of the position, we have revised the number and type of groups used to provide for greater homogeneity within each group.

The changes resulting from Phase II of the Stocktake were taken into account in this valuation and led to a reduction of about 30% in future service rates. This is because the changes were law as at 1st April 2005. On 13th July 2005, the ODPM announced that the changes would be revoked with retrospective effect from 1st April 2005. At the time of writing, we are considering the impact of this revocation on the solvency of the Fund.

# Statement of the Actuary

## Introduction

The Local Government Pension Scheme Regulations 1997 require that a full actuarial valuation is carried out every third year. The purpose of this is to establish that the Tyne and Wear Pension Fund (the Fund) is able to meet its liabilities to past and present contributors and to review employer contribution rates. The last full actuarial investigation into the financial position of the Fund, in accordance with Regulation 77(1) of the Scheme Regulations, was completed as at 31st March 2004.

## Actuarial Position

1. Rates of contributions paid by the participating Employers during 2004/05 were based on the actuarial valuation carried out as at 31st March 2001.

2. That valuation showed that the required level of contributions to be paid to the Fund by participating Employers (in aggregate) with effect from 1st April 2002 was as set out below:

- *210% of members' contributions to meet the liabilities arising in respect of service after the valuation date.*

### Plus

- *125% of members' contributions to restore the assets to 100% of the liabilities in respect of service prior to the valuation date, over a recovery period of 13 years.*

### Less

- *20% of members' contributions in respect of higher assumed investment income over the short term.*

3. Actual rates of contribution payable by each employer were set out in the Actuary's certificate dated March 2002.

4. The valuation as at 31st March 2004 showed that the financial position of the Fund had deteriorated since the previous valuation with the market value of the Fund's assets, after application of a smoothing adjustment, covering 64% of the liabilities allowing, in the case of current contributors to the Fund, for future increases in pensionable remuneration.

5. The valuation also showed that the required level of contributions to be paid to the Fund by participating Employers (in aggregate) with effect from 1st April 2005 was as set out below:

- *240% of members' contributions to meet the liabilities arising in respect of service after the valuation date.*

### Plus

- *140% of members' contributions to restore the assets to 100% of the liabilities in respect of service prior to the valuation date, over a recovery period of 25 years.*

### Less

- *35% of members' contributions in respect of higher assumed investment income over the short term.*

*These figures are based on the Regulations in force at the time of signing the valuation report.*

The majority of Employers participating in the Fund pay different rates of contributions depending on their past experience, their current staff profile, and the recovery period agreed with the Administering Authority. For many Employers, where the valuation indicated a significant increase in contributions from 1st April 2005, the Administering Authority has agreed with the employer that increases will be stepped over a period not exceeding 3 years.

If the assumptions are borne out in practice, the rate of contribution for each Employer would be expected to continue stepping up to the end of the relevant stepping period. The rate would then increase, due to the cessation of the short term additional investment income, and continue at the resultant level for the balance of the relevant recovery period before reverting to the relevant long term rate. In practice, contribution rates will be reviewed at the next valuation due at 31 March 2007 and further assumptions may be made at that time concerning short term investment returns.

6. The rates of contributions payable by each participating Employer over the period 1st April 2005 to 31st March 2008 are set out in a certificate dated 30th March 2005 which is appended to our report of the same date on the actuarial valuation.
7. The contribution rates were calculated using the projected unit actuarial method and the main actuarial assumptions are shown in the table below.

8. The next actuarial valuation of the Fund will be carried out as at 31st March 2007.
9. This statement has been prepared by the Actuary to the Fund, Hewitt Bacon & Woodrow for inclusion in the accounts of the Tyne and Wear Pension Fund. It provides a summary of the results of the actuarial valuation which was carried out as at 31st March 2004. The valuation provides a snapshot of the funding position at the valuation date and is used to assess the future level of contributions required.

This statement must not be considered without reference to the formal valuation report which details fully the context and limitations of the actuarial valuation.

Hewitt Bacon & Woodrow does not accept any responsibility or liability to any party other than our client, the Council of the Borough of South Tyneside, in respect of this statement.

<b>Discount rate for periods</b>	
In service	6.2% per annum
Left service	5.2% per annum
<b>Rate of general pay increases</b>	4.4% per annum
<b>Rate of increases to pensions in payment (in excess of Guaranteed Minimum Pensions)</b>	2.9% per annum
<b>Short term return on equities/property</b>	6.45% per annum
<b>Short term return on other assets</b>	5.2% per annum
<b>Valuation of assets</b>	smoothed market value.

## Membership of the Fund

As at 31st March 2005, there were 116 employers 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.

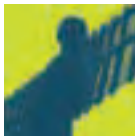




A number of employers outsourced parts of their functions during the year. The transferred employees have continued to be Scheme members where the contractor has been admitted to the Fund.

The Fund had 94,153 members at the year end, as set out below:

<b>Current Contributors</b>	<b>48,660</b>
<b>Deferred Members</b>	<b>16,471</b>
<b>Pensioners</b>	<b>29,022</b>
<b>Total Membership</b>	<b>94,153</b>

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Employers in the Fund and their members as at the 31st March 2005 are as follows:

<b>District Councils</b>	<b>Contributors</b>	<b>Deferreds</b>	<b>Pensioners</b>
 Gateshead Council	8,045	2,303	4,668
 Newcastle City Council	8,707	3,077	6,463
 North Tyneside Council	5,897	2,116	3,627
 South Tyneside Council	5,768	1,850	3,256
 City of Sunderland Council	8,886	3,136	5,348
<b>Sub Totals</b>	<b>37,303</b>	<b>12,482</b>	<b>23,362</b>

<b>Other Scheduled Bodies</b>	<b>Contributors</b>	<b>Deferreds</b>	<b>Pensioners</b>
City of Sunderland College	495	90	46
Former North East Regional Airport	0	0	36
Former Tyne and Wear County Council	0	106	290
Former Tyne and Wear Residuary Body	0	6	30
Gateshead College	250	95	35
Gateshead Housing Company	288	9	4
Monkwearmouth College	0	1	5
National Probation Service - Northumbria	686	156	267
Newcastle College	523	153	96
Newcastle Education Action Zone	0	4	2
North Tyneside College	0	50	21
Northumberland Magistrates Court	0	45	82
Northumbria Police Authority	1,768	552	882
Northumbria University	1,457	555	424
South Tyneside College	261	85	92
South Tyneside Education Action Zone	0	2	0
Sunderland Education Action Zone	2	0	1
Tyne and Wear Fire and Civil Defence Authority	261	71	168
Tyne and Wear Passenger Transport Authority	96	27	79
Tyne Metropolitan College	218	0	0
Tynemouth College	0	22	6
University of Sunderland	883	399	257
Wearside College	0	5	8
Your Homes Newcastle	474	4	12
<b>Sub Totals</b>	<b>7,662</b>	<b>2,437</b>	<b>2,843</b>

<b>Resolution Bodies</b>	<b>Contributors</b>	<b>Deferreds</b>	<b>Pensioners</b>
Birtley Town Council	6	3	5
Blakelaw and North Fenham Parish	1	0	0
Blue Square Trading	13	3	0
Learning World	3	7	0
Nexus	985	419	1,396
<b>Sub Totals</b>	<b>1,008</b>	<b>432</b>	<b>1,401</b>

Admitted Bodies	Contributors	Deferreds	Pensioners
Age Concern Newcastle	76	20	19
AQA	0	3	12
Association of North East Councils	30	5	2
Baltic Arts Flour Mills Visual Arts Trust	5	4	0
Benton Grange School	0	0	8
Benwell Young Peoples Development Group	2	0	0
Bovis Lend Lease (BLL)	9	0	0
Brunswick Young Peoples Project	2	2	0
Catholic Care North East	0	24	27
Compass Group UK and Ireland Limited	5	0	0
Disability North	24	14	3
Gateshead Law Centre	9	5	0
Hebburn Neighbourhood Advice Centre	4	0	0
Higher Education Funding Council for England	0	2	8
Information North (Northern Regional Library System)	0	0	2
International Centre for Life	13	7	2
Jarvis Accommodation Services Limited	6	0	0
Jarvis-Sandhill View	7	1	0
Kenton Park Sports Centre	2	4	0
Managed Business Space Limited	2	0	0
Mitie Cleaning (North) Limited	0	1	0
Mitie PFI Limited	2	0	0
Morrison Facilities Services Limited	0	0	1
National Car Parks Limited	10	2	1
National Glass Centre	1	0	1
Newcastle Family Service Unit	0	4	3
Newcastle Healthy City Project	20	2	0
Newcastle International Airport Company Limited	258	251	294
Newcastle Law Centre	7	2	2
Newcastle Tenants Federation	3	4	1
Newcastle Theatre Royal Trust Limited	50	20	15
Newcastle West End Partnership	0	2	0
Newcastle Youth Congress	2	2	0
No Limits Theatre	2	0	0
Norcare	0	1	1
Norland Road Community Centre	0	1	0
North East Innovation Centre Company Limited	13	12	8
North East Museums, Libraries and Archives Council	21	1	4
North East Regional Employers Organisation	8	1	5
North Tyneside Child Care Enterprise	4	14	1
North Tyneside City Challenge	0	7	1
North Tyneside Disability Advice Centre	0	0	1
Northern Arts Association	0	42	8

	Contributors	Deferreds	Pensioners
Northern Council for Further Education	1	14	12
Northern Counties School	37	20	18
Northern Informatics Application Agency	0	0	0
Northumbria Tourist Board	0	41	9
One North East	0	3	6
Ouseburn Trust	0	2	0
Passenger Transport Company	0	0	96
Port of Tyne Authority	0	0	7
Praxis Service	1	3	0
Raich Carter Sports Complex	36	1	0
Saint Mary Magdalene and Holy Jesus Trust	8	5	3
Saint Mary the Virgin Estate Management Charity	0	0	1
Scolarest	18	0	0
Search Project	4	0	2
Simonside Community Centre	1	0	0
South Tyneside Groundwork Trust	5	3	2
South Tyneside Victim Support	0	2	0
Southern Electric Contracting Limited	0	0	0
Stagecoach Travel Services (Busways)	255	212	528
Sunderland City Training and Enterprise Council	0	49	19
Sunderland Empire Theatre Trust Limited	0	7	4
Sunderland Housing Group	1,525	146	102
Sunderland Outdoor Activities Association	0	3	0
Sunderland Streetlighting Limited	60	1	1
The Ozanam House Probation Hostel Committee	21	8	4
Thomas Gaughan Community Association	3	0	0
Tyne and Wear Development Company Limited	13	11	2
Tyne and Wear Development Corporation	0	30	22
Tyne and Wear Enterprise Trust Limited	21	11	12
Tyne and Wear Play Association	1	0	0
Tyne and Wear Small Business Service	46	5	3
Tyne Waste Limited	0	12	10
Tyneside Deaf Youth Project	4	0	0
Tyneside Training and Enterprise Council	0	47	29
Valley Citizens Advice Bureau	0	2	0
Walker Profiles (North East) Limited	30	0	0
Wallsend Citizens Advice Centre	0	2	1
Wallsend Peoples Centre	0	3	2
Workshops for the Adult Blind (Palatine Products)	0	17	91
<b>Sub Totals</b>	<b>2,687</b>	<b>1,120</b>	<b>1,416</b>
<b>Grand Totals</b>	<b>48,660</b>	<b>16,471</b>	<b>29,022</b>

# Services to Members and Employers

## Introduction

The provision of a pensions service to 94,000 members and 116 employers is a substantial undertaking. In order to provide this service the Pensions Office is organised into five teams that are comprised of experienced officers who have the opportunity and are encouraged to obtain a recognised professional pensions qualification.

A Communications Team prepares and provides Scheme and Fund specific information and manages contact with employers and members.

Our Technical Team provides support to these four teams, with particular regard to the Scheme's regulatory background, financial control and IT systems and solutions.

We have prepared and published a set of Service Standards that set out the services we provide to members and employers. These are included in this Annual Report on pages 42 to 43.

## Services to Members

Some of the features of the service we provide to members are set out below:

- We maintain a website, for which the address is [www.twpf.info](http://www.twpf.info).
- We provide a dedicated members Helpline which received almost 50,000 calls in 2004/05. This is an increase of 14,000 over the previous year.
- We provide annual benefit statements for current contributors and deferred members. This is sent direct to their home address, accompanied by the Members' Annual Report.
- We provide additional newsletters to keep members informed of the ongoing changes to the Scheme.
- We send a letter to our pensioners detailing the annual increase to their pension.
- The Members' Annual report is also provided.
- We offer seminars to members on request. Over 660 members attended the 33 seminars that were held in 2004/05.

- We provide a comprehensive range of information booklets that are available on our website or on request from the Helpline.

All information supplied by the Fund is available on request in a range of formats including other languages, large print and Braille. We also have access to audio aids and British Sign Language interpretation services. On joining the Fund, members can register to receive all future information in their preferred format.

## Annual Benefit Statements

Since 1999 the Fund has produced annual benefit statements for its current contributors that set out current and projected Scheme benefits. In 2004, the Fund worked in partnership with the Department of Work and Pensions on a pilot scheme for combined benefit statements. This pilot was targeted on 10% of our current contributors, who received information on their current and projected State Pension entitlement in addition to the statement on Scheme benefits. The pilot was successful and we are working to provide all current contributors with a combined benefit statement in 2005.

Statements were introduced for deferred members on request in 2003. From 2004, we have produced statements for all deferred members for whom we believe we hold a reliable address.

## Services to Employers

The Services that we provide to employers includes the following initiatives:

- We provide each employer with a client manager whose role it is to ensure efficient processing and communication.
- We have introduced a programme of regular meetings for all employers at which issues related to pensions administration are discussed.
- We provide an Employers' Guide to the administration of the Fund.



- We offer training courses that aim to educate and inform staff on pension matters and working procedures. In the past year we provided training to 23 representatives from 6 employers.
- We have a Partnership Agreement that sets out our respective roles and responsibilities.
- We host an annual general meeting.
- We send out mailshots to advise employers of developments.
- The website has a dedicated password protected area for employers. So far the 5 local authorities and 23 other employers have registered to use our on line services. Further details are given below.

### Satisfaction Surveys

The Fund is committed to continually improving its services to members and employers. We seek their views on the service through surveys.

In 2004/05, we issued surveys to our current contributors and employers. We were pleased to see that 98% of our current contributors stated they were satisfied with the service we provide, as did 92% of the employers who responded. A number of helpful comments were made on service provision which have received consideration.

### The Website and Electronic Communication

The Fund's website [www.twpf.info](http://www.twpf.info) is increasingly important to our service delivery package. We are committed to continually developing and improving this means of communication.

Through the website, members have access to:

- Details on how to contact the Fund.
- Make comment about the Fund.
- Latest news and topical issues.
- Information booklets.

- Pension payment dates and details of pension inflation proofing.
- Links to other useful websites.
- Pensions Committee reports.
- Current and previous years Annual Report and Accounts.
- The Statement of Investment Principles and the Policy on Socially Responsible Investment.

A password protected secure area for employers can be accessed via the Fund's main website. After an initial registration process, employers have access to:

- The pension records of their own employees.
- The Employers' Guide.
- Templates of administration forms.
- Latest news and topical issues.
- Pension Committee reports.

The Fund is working to expand the interactive nature of the website. We intend to introduce systems that allow members to view their personal record and to calculate estimates of existing benefits and possible improvements to their benefits. We are also looking to introduce on-line automated data transmission and processing for Employers.

The Fund promotes and encourages the use of email as a means of communication. We are looking to develop the use of email alerts to employers for important news and latest information.

We can be contacted at [pensions@twpf.info](mailto:pensions@twpf.info)

### Equality and Diversity

We are committed to equality and diversity within our service delivery and employment practices. The Council has achieved Level 1 of the Equality Standard for Local Government and is working to achieve Level 2 by December 2005.

# 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.

## Strategic Investment Policy

The 2004/05 strategic investment policy is derived from an asset liability study that was first undertaken in 2000. 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.

The study indicated that a diversified portfolio invested 65% in Equities, 27.5% in Bonds and 7.5% in Property represented a suitable strategic benchmark for the Fund.

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 resourced out of the allocation to Equities.

The benchmark is:

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

The outcome of this initial study was tested against updated investment data and rolled forward liability data in each year to 2003/04 and was found to remain appropriate. This ongoing exercise has ensured that the Fund has been properly invested in relation to its liabilities and to opportunities in investment markets.

The benchmark has been subject to a fundamental review during 2004/05. This was undertaken by the Fund's Investment Advisor, Hymans Robertson, and has used the liability data from the 2004 Actuarial Valuation.

This review has determined that the optimal investment strategy for the Fund, going forward, is 67.5% in Equities, 22.5% in Bonds and 10% in Property. This represents increases of 2.5% in both Equities and Property, funded by a reduction in the Bonds exposure of 5%. The allocation to Private Equity remains unchanged at 5%.

A summary of the changes to the strategic benchmark are shown below.

The table shows that there will be a 5% increase in the allocation to Overseas Equities, which will bring the exposure to this asset class to 40%. This increased allocation increases the currency risk within the Fund and consideration is being given to putting a currency management strategy in place.

The changes to the benchmark are being implemented in 2005/06.

Asset Class	Strategic Benchmark 2004/05	Strategic Benchmark 2005/06 onwards	Change in Strategic Benchmark
<b>UK Equities</b>	<b>30.00</b>	<b>27.50</b>	<b>-2.50</b>
<b>Overseas Equities</b>	<b>35.00</b>	<b>40.00</b>	<b>+5.00</b>
US	9.75	12.50	+2.75
Europe ex UK	12.25	13.50	+1.25
Japan	6.50	7.00	+0.50
Other Far East	3.25	3.50	+0.25
Emerging Markets	3.25	3.50	+0.25
<b>Total Equities</b>	<b>65.00</b>	<b>67.50</b>	<b>+2.50</b>
<b>Fixed Interest</b>	<b>27.50</b>	<b>22.50</b>	<b>-5.00</b>
UK Gilts	8.75	7.00	-1.75
UK Index-Linked	5.00	4.00	-1.00
Sterling Non Government	11.00	9.00	-2.00
Overseas	2.75	2.50	-0.25
<b>Property</b>	<b>7.50</b>	<b>10.00</b>	<b>+2.50</b>

## Investment Management Structure

The Fund employs eight specialist managers over thirteen investment mandates. This broadly based structure ensures that investment returns are not overly influenced by the performance of any one manager.

Manager	Portfolio
Legal & General	Indexation <ul style="list-style-type: none"> <li>• UK Equities</li> <li>• US Equities</li> <li>• Corporate Bonds</li> <li>• UK Index-Linked</li> </ul>
Capital	Global Equities Emerging Market Equities
UBS	Pan European Equities
Fidelity	UK Equities
Schroder	Japanese Equities Pacific Rim ex Japan Equities
Prudential M&G	Corporate Bonds
Henderson	Global Government Bonds
Arlington	Property

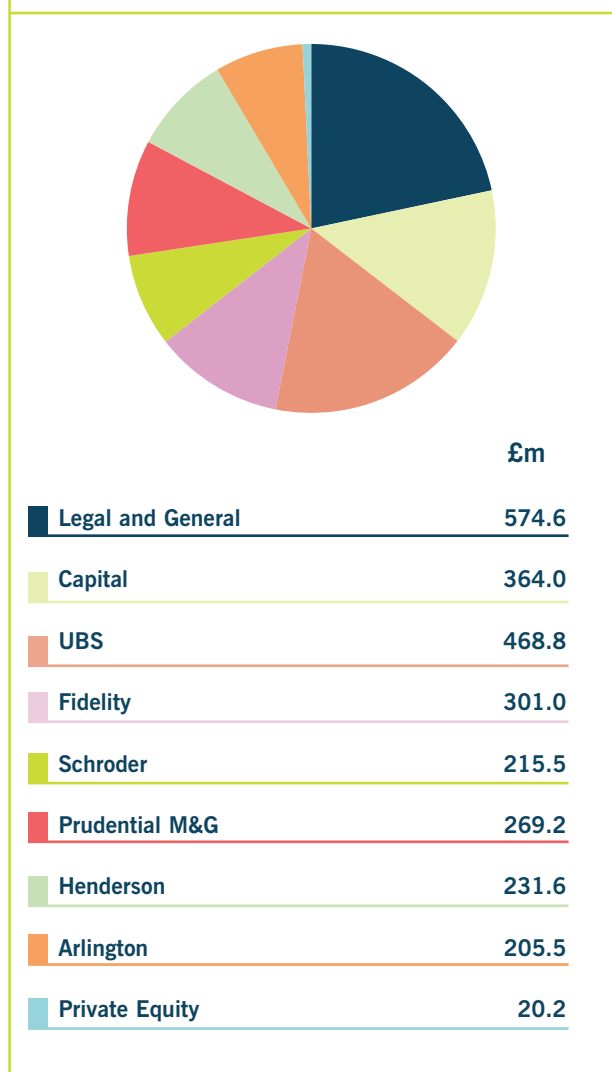
When this investment management structure was being designed and implemented, consideration was given to its flexibility and resilience to change. Consequently, the Fund's new benchmark may be implemented largely through the existing line up of managers. One or more specialist currency managers may be appointed to implement a currency strategy.

As noted earlier, the Fund is building up to a 5% weighting in Private Equity. So far, the programme has been largely comprised of fund of funds investments with HarbourVest. In order to diversify this exposure and to speed up progress towards attaining the target weighting, the Fund has

considered investing with other Private Equity providers that would complement the programme with HarbourVest.

During the year, the Fund has made a commitment to an Emerging Markets Fund raised by Capital International. A decision has also been taken to make commitments to a range of global fund of funds managed by Pantheon Ventures and a secondary fund managed by Lexington Partners.

**The value of assets with each manager and invested in Private Equity at the year end is:**



## 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 appropriate indices, which generally require outperformance over three year rolling periods. Annual downside targets have also been set.

Investment in Private Equity is made largely on a fund of funds basis. Whilst an outperformance target of 5% above Quoted Equity has been set, official measurement against this target is inappropriate at this early stage of investment into the asset class.

The Property Portfolio has a target based on the Investment Property Databank (IPD) Index.

## Custody

The Fund has reviewed its custody arrangements during the year. It has been decided to consolidate the custody of the segregated assets with Northern Trust.

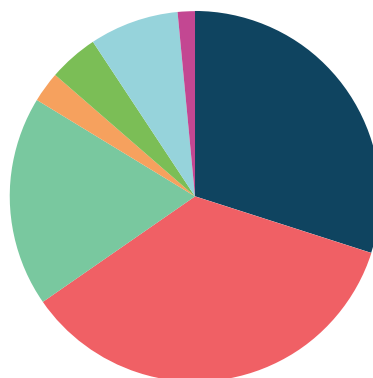
Northern Trust was initially appointed in 2002 to provide custody services for four mandates. Under the new arrangements, Northern Trust provides custody for approximately £1.6 million of segregated assets held in eight mandates.

## Investment Strategy

The asset allocation is maintained within pre-determined ranges around the strategic benchmark. When a range is breached, the Fund is rebalanced back within the ranges. Legal and General assists with this process by providing management information.

Those active managers that invest in more than one market are permitted to make tactical asset allocation decisions within their portfolios. This does not impact on the Fund's overall strategy but provides additional scope for managers to outperform their targets.

### The asset allocation at the year end is:



	£m	%
<b>UK Equities</b>	<b>796.2</b>	<b>29.9</b>
<b>Overseas Equities</b>	<b>941.9</b>	<b>35.4</b>
<b>UK Fixed Interest</b>	<b>488.1</b>	<b>18.4</b>
<b>Overseas Fixed Interest</b>	<b>71.7</b>	<b>2.7</b>
<b>Index Linked</b>	<b>115.0</b>	<b>4.3</b>
<b>Property</b>	<b>207.5</b>	<b>7.8</b>
<b>Net Current Assets</b>	<b>41.1</b>	<b>1.5</b>

### Performance Measurement

2004/05 is the third year for which performance has been measured against the Fund specific strategic benchmark. A hybrid benchmark is used for longer periods that end on 31st March 2005. This is based on the median up to and including periods ending on 31st January 2002 and on the strategic benchmark thereafter.

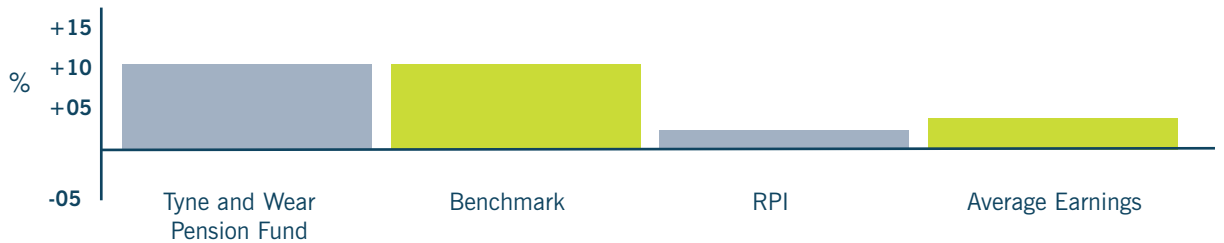
### Returns for 2004/05

Equity markets rose over the past year, thereby consolidating impressive gains since the low point in markets in March 2003. This period of recovery followed three years of negative returns during

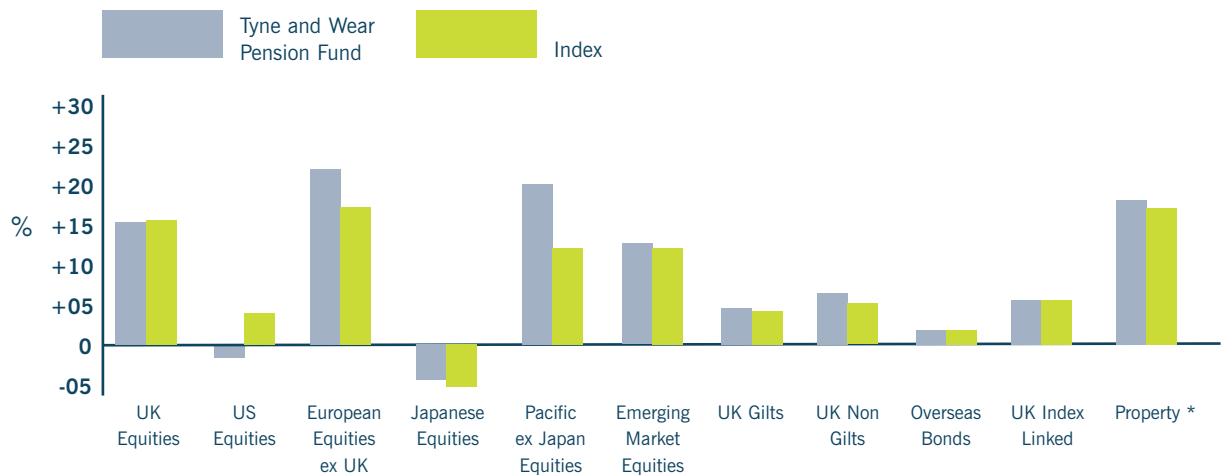
which Equity values declined significantly from the high point attained in early 2000. However, Equity markets are still valued about 30% below the peak of the market.

In this environment, pension funds have been able to post good positive returns for the second year in succession. The year started with continued confidence that the global economy was improving and this led to a rise in Equity markets. However, some concerns surfaced towards the end of the year over a US led slowdown. With the exception of the Japanese market, all of the major Equity markets posted positive returns.

The Fund's return for the year was 10.9%, which was in line with the benchmark.



The chart shows the Fund's returns over the main investment markets for 2004/05.



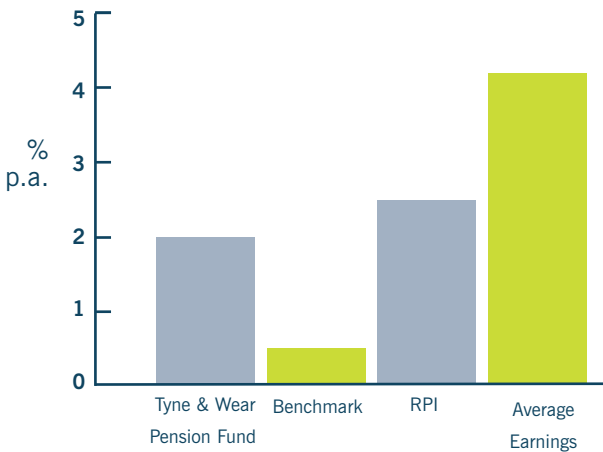
\* Property performance is measured and shown on a calendar year basis to 31st December 2004.

## Five Year Performance

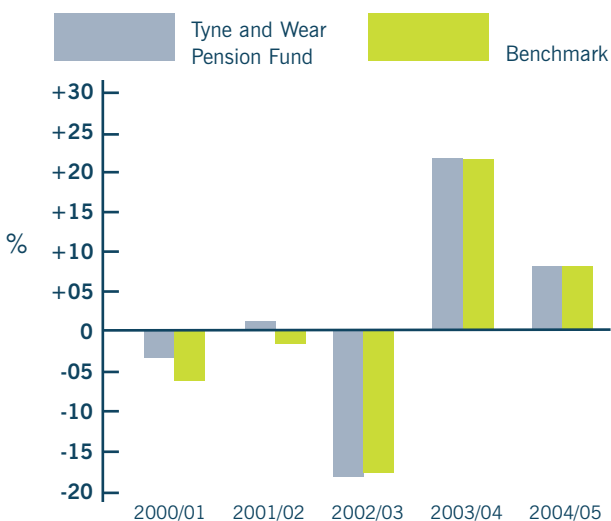
In order to avoid taking too short term a view of investment performance, pension fund returns are generally assessed over five year periods. The Fund's annual return over the last five years has been 2.0% per annum. The decline in Equity markets from March 2000 to March 2003 is the main reason for this low return.

Whilst this return is disappointing in absolute terms and lags both inflation and the increase in average earnings over the period, it is pleasing to note that it is above the benchmark return of 0.5% per annum.

Annualised Five Year Performance to 31st March 2005.



The annual performance of the Fund, relative to the benchmark, can be broken down into individual years.



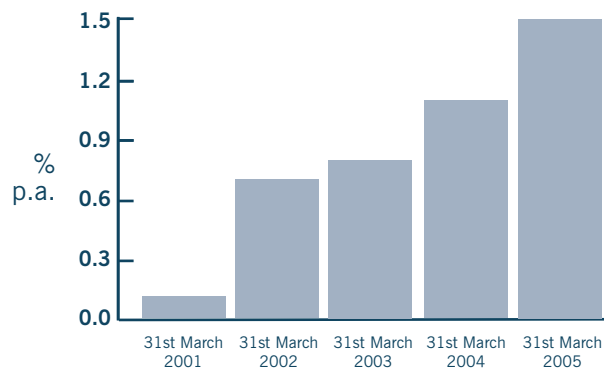
The chart shows that the Fund has outperformed for the first two years of the period. At that time, the Fund had a defensive asset allocation. Equity markets performed very poorly during this period and this defensive stance assisted returns.

In 2002/03, the Fund's manager's started to reposition their portfolios for an Equity market recovery. This did not come through in that year so the Fund underperformed. However, the expected recovery did come through in 2003/04, which led to another year of outperformance. During 2004/05 the Fund performed in line with the benchmark.

The five year rolling performance has been showing a steady improvement since March 2000.

The chart below shows this improvement, with the Fund outperforming in each of the rolling periods.

Relative Annualised Performance for Five Year Periods Ending 31st March 2001 to 31st March 2005.



# 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 voluntary, legislation requires local government pension funds to state the extent of their compliance.

Last year, the Fund was able to report full compliance with all ten of the Myners Principles. Full compliance has been maintained during 2004/05.

A summary of the Principles and the Fund’s compliance is shown below.

<p><b>Principle 1</b> – Decisions should only be taken by those with sufficient expertise.</p>	<p><b>Fully Compliant.</b> An Investment Panel provides increased focus and scrutiny over investment decisions. A comprehensive training programme is in place for Pensions Committee Members. A Committee Members Handbook has been issued.</p>
<p><b>Principle 2</b> – Clear investment objectives should be set.</p>	<p><b>Fully Compliant.</b> The Fund has set formal investment objectives.</p>
<p><b>Principle 3</b> – Strategic asset allocation decisions should receive sufficient attention.</p>	<p><b>Fully Compliant.</b> The Fund has undertaken an asset liability study and tests the results annually in the light of changing market and liability data.</p>
<p><b>Principle 4</b> – Contracts for actuarial services and investment advice should be open to separate competition.</p>	<p><b>Fully Compliant.</b> The actuarial services contract and the investment advisory contract were separately tendered in 2003/04.</p>
<p><b>Principle 5</b> – An explicit written mandate should be agreed between the Fund and the investment managers and transaction related costs should be monitored.</p>	<p><b>Fully Compliant.</b> Written mandates have been agreed with all investment managers and arrangements have been put in place to monitor transaction costs.</p>
<p><b>Principle 6</b> – The Fund should play an active role in Corporate Governance.</p>	<p><b>Fully Compliant.</b> The Fund has a policy on Socially Responsible Investment, the Exercise of Rights and Corporate Governance.</p>
<p><b>Principle 7</b> – The Fund should set appropriate investment benchmarks.</p>	<p><b>Fully Compliant.</b> Investment benchmarks have been set for the Total Fund and for individual investment mandates.</p>
<p><b>Principle 8</b> – Arrangements should be made to measure the performance of the Fund, the Committee, Advisors and Managers.</p>	<p><b>Fully Compliant.</b> A service provider has been appointed to measure the risk and return of the Total Fund and of individual managers. A formal assessment of the effectiveness of decisions taken by the Committee, the Advisor and the Officers takes place. The decision making process has been subject to independent review.</p>
<p><b>Principle 9</b> – The Statement of Investment (SIP) Principles should be strengthened.</p>	<p><b>Fully Compliant.</b> The Fund’s SIP has been expanded to include all of the areas required by the Myners Report.</p>
<p><b>Principle 10</b> – The Fund should publish its SIP and the results of monitoring.</p>	<p><b>Fully Compliant.</b> The Fund’s SIP is published in the Annual Report and Accounts and is available on the fund’s website <a href="http://www.twpf.info">www.twpf.info</a></p>



## 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 Fund's SIP is a key document. It sets out the investment framework and provides an up to date assessment of compliance with the Investment Principles. The document is reviewed as new developments take place and was last updated as at 7th June 2005.

### The SIP sets out the following details:

- 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 advisors and managers.
- The nature of the fee structures in place for advisors 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 44 to 50.

## 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 and by the Responsibilities of Institutional Shareholders and Agents – Statement of Principles, prepared by the Institutional Shareholders Committee in 2002.
- The approach towards companies outside the UK to take account of the practices of the home nation.
- The approach towards unquoted companies to be consistent with the approach adopted for quoted companies, to the extent that this is practicable.
- Voting rights to 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.

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

In 2004 the Fund joined the Local Authority Pension Fund Forum. The Forum is comprised of about 30 local authority pension funds with total assets of around £40 billion. The Forum is committed to actively encouraging companies to comply with good practice on corporate governance and Socially Responsible Investment issues. By doing so it believes that shareholder value is improved over the medium and longer term. The Forum also believes that a coordinated approach with other local authority funds will increase the level of effectiveness when seeking change.

### **Socially Responsible Investment**

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 is combined with the policy on voting and corporate governance in a document entitled "Policy on Socially Responsible Investment, the Exercise of Rights and Corporate Governance". It 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 June 2005. A copy is shown on pages 51 to 52.

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 meetings with investment managers.



Last year, the Fund was able to report full compliance with all ten of the Myners Principles. Full compliance has been maintained during 2004/05.



# Financial Statements

Fund Account					
2003/2004			Note	2004/2005	
£'000	£'000			£'000	£'000
<b>Contributions and Benefits</b>					
172,573		Contributions Receivable	3	183,686	
<u>14,875</u>		Transfers In	4	<u>21,355</u>	
	187,448				205,041
<b>Returns on investments</b>					
113,889		Benefits Payable	5	118,568	
16,110		Out (Leavers)	6	18,845	
<u>2,112</u>		Administrative Expenses	7	<u>2,080</u>	
	<u>132,111</u>				<u>139,493</u>
	<b>55,337</b>	<b>Net Additions from Dealings with Members</b>			<b>65,548</b>
50,345		Investment Income	8	52,842	
-2,435		Non Recoverable Tax	8	-3,386	
392,068		Change in Market Value of Investments	9	209,139	
-4,755		Investment Management Expenses	10	-5,292	
	<u>435,223</u>	<b>Net Returns on Investments</b>			<u>253,303</u>
	490,560	<b>Net Increase/(Decrease) in the Fund During the Year</b>			318,851
	<u>1,865,116</u>	<b>Net Assets of the Fund at 1st April</b>			<u>2,355,676</u>
	<b><u>2,355,676</u></b>	<b>Net Assets of the Fund at 31st March</b>			<b><u>2,674,527</u></b>

## Net Assets Statement

2003/2004			Note	2004/2005	
£'000	£'000			£'000	£'000
		<b>Investments</b>	<b>9</b>		
233,879		Fixed Interest Securities		244,432	
1,133,546		Equities		1,296,384	
15,152		Index-Linked Securities		17,450	
767,307		Pooled Investment Vehicles		854,595	
157,740		Properties		207,479	
25,274		Cash Deposits		36,539	
<u>7,651</u>		Other investment balances		<u>4,636</u>	
	2,340,549				2,661,515
	<u>15,127</u>	<b>Current Assets and Liabilities</b>	<b>11</b>		<u>13,012</u>
	<u><b>2,355,676</b></u>	<b>Net Assets of the Fund at 31st March</b>			<u><b>2,674,527</b></u>

# 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 2004 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 the statement prepared by the Actuary, which is shown on pages 14 and 15. The financial statements should be read in conjunction with the Actuary's statement.

## 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 31st March 2005.

Unitised securities have been included at the average of their bid and offer prices on 31st March 2005.

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

The value of fixed income investments excludes interest earned but not paid over at the year end. This interest earned has been accrued within investment income. This represents a change to accounting policy in 2004/05. Previously, the value of fixed income investments has included interest earned but not paid over at the year end.

Accordingly, the figures for 2003/04 have been restated to take account of the new accounting policy. Within the Fund Account, Investment Income has been increased by £0.285 million with a corresponding reduction in the Change in Market Value figure. Within the Net Assets Statement the value of Fixed Interest Securities has been reduced by £3.603 million and Index-Linked Securities reduced by £0.119 million. The value of Other Investment Balances has been increased by £3.722 million to reflect a corresponding increase in debtors.

Overseas investments and foreign currency balances have been converted into Sterling at the closing exchange rates on 31st March 2005.

Properties are shown as valued at 31st December 2004, with the exception of three properties purchased after that date which have been valued at cost. The valuers are Fellows of the Royal Institute of Chartered Surveyors from Lambert Smith Hampton.

### Investment Transactions

Investment transactions that were not settled as at 31st March 2005 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 31st March 2005.

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 2005 is credited to the Fund Account.

Interest on cash deposits has been accrued up to 31st March 2005.

### Investment Management Expenses

Investment management expenses payable as at 31st March 2005 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 2005.

### Contributions

Contributions represent the amounts received 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 2005 have been accrued.

### Benefits and Refunds

Benefits and refunds are accounted for in the year in which they become due for payment.

### Transfer Values

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

Contributions receivable are analysed below:

	2004/2005	2003/2004
	£'000	£'000
<b>Employers</b>		
Normal	86,105	80,250
Additional	52,117	49,841
<b>Members</b>		
Normal	44,820	41,818
In-House AVCs	644	664
	<b>183,686</b>	<b>172,573</b>

The contributions can be analysed by type of member body as follows:

	2004/2005	2003/2004
	£'000	£'000
Administering Authority	20,967	18,737
Other District Councils	115,066	109,959
Other Scheduled Bodies	28,339	23,840
Resolution Bodies	6,361	6,693
Admitted Bodies	12,953	13,344
	<b>183,686</b>	<b>172,573</b>

#### 4. Transfers In

During the year individual transfers in from other schemes amounted to £21.355 million (£14.875 million in 2003/04).

#### 5. Benefits Payable

	2004/2005 £'000	2003/2004 £'000
Pensions	111,029	106,096
Commutations and Lump Sum Retirement Benefits	15,314	16,415
Lump Sum Death Benefits	2,116	1,883
Less: Recharges	-9,891	-10,505
	<b>118,568</b>	<b>113,889</b>

The analysis of benefits by type of member body is not available. In this respect the accounts do not comply with the 2004 Code of Practice on Local Authority Accounting.

#### 6. Payments To And On Account Of Leavers

	2004/2005 £'000	2003/2004 £'000
Individual Transfers to Other Schemes	18,142	15,109
Refunds to Members Leaving Service	703	1,001
	<b>18,845</b>	<b>16,110</b>

#### 7. Administration Expenses

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 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 below:

	2004/2005 £'000	2003/2004 £'000
Employee Expenses	1,195	1,121
Support Services Recharge	638	676
Audit Commission Fees	17	16
External ICT Costs	40	105
Printing/Publications	100	81
Professional Fees	132	88
Other Expenses	55	91
SIB Pension Review	- 29	-26
Other Income	- 68	-40
	<b>2,080</b>	<b>2,112</b>

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



## 8. Investment Income

	2004/2005	2003/2004
	£'000	£'000
Fixed Interest Securities	8,515	10,940
Equities	32,498	27,408
Index-Linked Securities	360	571
Pooled Investment Vehicles	67	44
Properties – Net Rents	9,263	10,131
Cash Deposits	1,696	952
Securities Lending	166	6
Commission Recapture	277	279
Underwriting Commission	0	14
Sub-Total	52,842	50,345
Less: Non Recoverable Tax	-3,386	-2,435
Total Investment Income	49,456	47,910

## 9. Investments

	Value at 1.4.04 £'000	Purchases at Cost £'000	Sales Proceeds £'000	Change in Market Value £'000	Value at 31.3.05 £'000
Fixed Interest Securities	233,879	669,120	-662,149	3,582	244,432
Equities	1,133,546	505,224	-448,884	106,498	1,296,384
Index-Linked Securities	15,152	13,096	-11,552	754	17,450
Pooled Investment Vehicles	767,307	26,554	-16,237	76,971	854,595
Properties	157,740	50,568	-19,750	18,921	207,479
	2,307,624	1,264,562	-1,158,572	206,726	2,620,340
Cash Deposits	25,274	11,161	0	104	36,539
Other Investment Balances	7,651	7,716	-13,040	2,309	4,636
	2,340,549	1,283,439	-1,171,612	209,139	2,661,515

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.

	2004/2005	2003/2004
	£'000	£'000
<b>Fixed Interest Securities</b>		
UK Public Sector	130,116	124,495
UK Other	42,663	38,033
Overseas Public Sector	71,653	71,351
	244,432	233,879
<b>Equities</b>		
UK Quoted	479,083	432,183
UK Unquoted	0	2
Overseas Quoted	817,301	701,361
	1,296,384	1,133,546
<b>Index-Linked Securities</b>		
UK Quoted	17,450	15,152

	2004/2005 £'000	2003/2004 £'000
<b>Pooled Investment Vehicles</b>		
Unit Trusts	7,414	8,581
Unitised Insurance Policies	718,115	653,186
Other Managed Funds	129,066	105,540
	<b>854,595</b>	<b>767,307</b>
<b>Properties</b>		
Freehold	186,269	139,600
Long Leasehold	21,210	18,140
	<b>207,479</b>	<b>157,740</b>
<b>Cash Deposits</b>		
Sterling	26,154	22,613
Foreign Currency	10,385	2,661
	<b>36,539</b>	<b>25,274</b>
<b>Other Investment Balances</b>		
Currency Hedging	2,075	1,629
Debtors	20,261	12,549
Creditors	-17,700	-6,527
	<b>4,636</b>	<b>7,651</b>

## 10. Investment Management Expenses

The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 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:

	2004/2005 £'000	2003/2004 £'000
Administration, Management and Custody	5,099	4,606
Performance and Risk Measurement Services	60	69
Other Advisory Fees	116	64
Audit Fees	17	16
	<b>5,292</b>	<b>4,755</b>

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

	2004/2005 £'000	2003/2004 £'000
Contributions and Recharges Due	17,596	17,228
Inland Revenue	-2,047	-1,897
Investment Management Expenses	-1,233	-1,156
Other	-1,304	952
	<b>13,012</b>	<b>15,127</b>

## 12. Additional Voluntary Contributions (AVCs)

The Fund offers two types of AVC arrangements.

Additional years of service 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 has 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. Contributions to these external providers are invested separately from the Fund's own assets.

Equitable Life has been experiencing significant financial difficulties over the past few years. The problems arose from some of its financial products that carry guaranteed returns.

With the exception of existing life cover policies, the Fund has closed its' AVC plan with Equitable Life to new members and transfers. A significant proportion of investors in other funds operated by Equitable have had their balances transferred to The Prudential. The Fund continues to monitor the position of the remaining investors with Equitable.

As at 31st March 2005 the AVC funds provided by The Prudential were valued at £5.097 million (£4.451 million as at 31st March 2004) and the funds operated by Equitable Life were valued at £1.207 million (£1.331 million as at 31st March 2004). The funds are valued by each of the providers and take no account of accruals.

## 13. Analysis of Investments Over Managers

The Fund employs eight specialist external investment managers over a total of thirteen different 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 market value of investments in the hands of each manager was:

As at 31st March 2004		Investment Managers	As at 31st March 2005	
£'000	%		£'000	%
156,091	7	Arlington Property Investors	205,530	8
267,006	12	Capital International – Global Equities	290,524	11
67,033	3	Capital International – Emerging Markets	73,496	3
261,061	11	Fidelity Pensions Management	301,039	11
218,576	9	Henderson Global Investors	231,639	9
510,239	22	Legal & General Investment Management	574,566	21
260,936	11	Prudential M&G	269,205	10
204,713	9	Schroder Investment Management	215,503	8
382,390	16	UBS Global Asset Management	468,825	18
7,566	0	Private Equity	20,237	1
4,938	0	Managed In-House	10,951	0
<b>2,340,549</b>	<b>100</b>	<b>Total Investments</b>	<b>2,661,515</b>	<b>100</b>

## 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

The Fund has used Forward Currency Contracts to hedge the currency exposure on certain overseas investments. As at 31st March 2005, the Fund held a range of positions which together showed an unrealised profit of £2.075 million. Of the 56 positions open as at 31st March 2005, 39 have been settled showing an overall profit of £1.869 million. At the time of finalising the accounts 17 of these positions remained open. As at 31st May 2005 these positions are showing an unrealised profit of £1.670 million.

## 16. Securities Lending

The Fund started a securities lending programme in 2003/04, with the Fund's custodian, Northern Trust acting as a securities lending manager and collateral manager. In August 2004, the Fund also started lending securities through its custodial arrangements with UBS Asset Management.

In late 2004, the Fund reviewed its custody arrangements and decided to consolidate the custody of all segregated assets with Northern Trust. As a consequence, from 1st February 2005,

the lending arrangement with UBS was terminated and Northern Trust became responsible for all of the Fund's securities lending activities.

Securities totalling a value of £167.540 million were loaned out as at 31st March 2005, against collateral (in the form of financial instruments) of £175.341 million.

The breakdown of securities on loan as at 31st March 2005 is:

	2004/2005 £'000	2003/2004 £'000
Fixed Interest Securities	92,834	58,979
Index-Linked Securities	6,813	0
UK Equities	33,099	38,682
Overseas Equities	34,794	4,152
	<b>167,540</b>	<b>101,813</b>

## 17. Underwriting

The Fund accepts a number of underwriting and placing propositions. As at 31st March 2005, no commitments were outstanding.

## 18. Significant Holdings

As at 31st March 2005, 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 2005 this was valued at £493.130 million and represented 18.4% of the total net assets of the Fund.
- Prudential Pensions Limited Corporate Bond All Stocks Fund – as at 31st March 2005 this was valued at £215.174 million and represented 8.0% of the total net assets of the Fund.

## 19. Private Equity

As at 31st March 2005 the Fund had seven outstanding commitments to Private Equity Investments as follows:

As at 31st March 2005					
Name of Fund	Initial Commitment		Drawdowns made	Commitments Outstanding	
	Year	Value		Dollar	Sterling
HarbourVest International Private Equity Partners IV	2002	\$55.0m	\$20.5m	\$34.5m	£18.3m
HarbourVest Partners VII Cayman Buyout Fund	2002	\$46.0m	\$6.2m	\$39.8m	£21.1m
HarbourVest Partners VII Cayman Mezzanine Fund	2002	\$8.0m	\$0.8m	\$7.2m	£3.8m
HarbourVest Partners VII Cayman Venture Fund	2002	\$28.0m	\$3.2m	\$24.8m	£13.1m
HarbourVest Partners 2004 Direct Fund	2004	\$30.0m	\$3.7m	\$26.3m	£13.9m
Capital International Private Equity Fund IV	2004	\$18.0m	\$5.6m	\$12.4m	£6.6m
Capital North East	2002	£1.5m	£0.6m	N/A	£0.9m
<b>Total</b>					<b>£77.7m</b>

The Sterling figures noted above for the commitments outstanding as at 31st March 2005 are based on the Dollar/Sterling exchange rate at the close of business on that date.

## 20. Related Party Transactions

Under FRS8 "Related Party Disclosures" it is a requirement that material transactions with related parties, not disclosed elsewhere, should be included in a note to the financial statements.

Examinations of returns completed by Elected Members of the Pensions Committee and Senior Officers involved in the management of the Pension Fund have not identified any cases where disclosure is required.

During 2004/05 South Tyneside Council charged the Tyne and Wear Pension Fund £0.917 million (£0.916 million in 2003/04) in respect of services provided; primarily financial, legal and information technology. There were no material contributions due from employer bodies outstanding at the year end.

# Service Standards

We have prepared and published a set of Service Standards that set out the services we provide to members and employers.

## We will

- Provide you with a prompt, fair and efficient service.
- **Maintain high standards of financial control and security.**
- Maximise efficiency and minimise cost.
- **Be accountable for the service we provide.**
- Promote equality and diversity in the delivery of our services and in our employment practices.
- **Train and develop our staff so they can provide you with an excellent service.**
- Seek your views on how well we are meeting your needs and how we might improve the service.

## Services for Employers

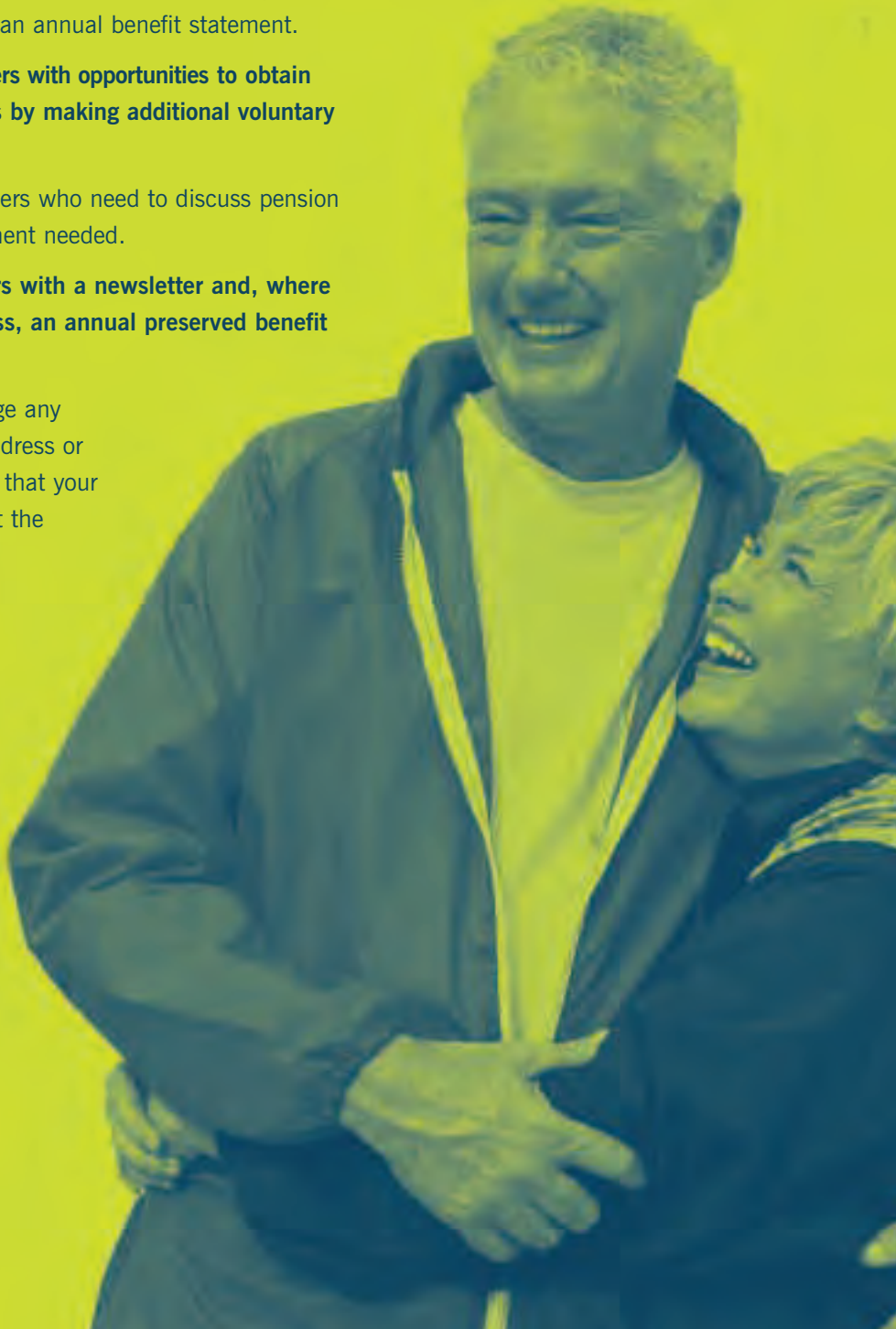
### We will

- **Encourage employers to enter into a Partnership Agreement that sets out the respective roles and responsibilities of employers and of the Fund.**
- Provide an Employers Guide that sets out guidance on pension matters.
- **Assist with your financial planning by undertaking interim valuations in the years between the statutory triennial valuations.**
- Provide you with a client manager who will be your first point of contact for any matters that you wish to raise.
- **Provide training for your staff who are involved in pensions administration.**
- Advise you of amendments to regulations and of other developments that may impact on you or your employees.
- **Host an annual meeting to report on the Fund's strategic position and to provide an opportunity for you to raise your concerns and issues.**
- Host an employers' forum to promote an ongoing discussion on investment and funding issues and provide this forum with representation on the Pensions Committee.
- **Host regular meetings with groups of employers to assist us all to administer the Fund efficiently.**
- Provide an employers' website through which you may link into the pensions administration system.
- **Work with you to improve the service offered to you and your employees.**
- Welcome visits from employers that need to discuss pensions issues with us.
- **Encourage prospective employers to join the Fund.**
- Advise you of consultation exercises and encourage you to make your views known.

## Services for Members

### We will

- Provide a welcome pack to new members.
- **Provide a comprehensive range of leaflets that explain the benefits and options available.**
- Provide a helpline to answer your questions about pension rights or options.
- **Provide a members' website.**
- Provide presentations on pensions issues to groups of members, on request.
- **Provide an annual fund report to all members.**
- Provide contributing members with a newsletter and, where we hold the necessary information, an annual benefit statement.
- **Provide contributing members with opportunities to obtain additional pension benefits by making additional voluntary contributions.**
- Welcome visits from members who need to discuss pension issues with us no appointment needed.
- **Provide preserved members with a newsletter and, where we hold the current address, an annual preserved benefit statement.**
- For pensioners, acknowledge any notification of change of address or banking details and ensure that your payroll record is updated at the earliest opportunity.
- **Advise pensioners, each April, of the annual statutory increase in the Local Government Pension.**



# Statement of Investment Principles

**Approved by Pensions Committee  
on 7th June 2005**

## Introduction

1. The Local Government Pension Scheme Regulations (the 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 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 Council (the 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 eighteen members. The Council nominates eight members and the other four district councils within the County area nominate one member each. The trades unions and the employers (excluding the district councils) each 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 that reviews and scrutinises the decisions and actions of the Pensions Committee.

9. A training programme is provided for members of both committees.
10. Hewitt Bacon and Woodrow has been appointed as Actuary.
11. Hymans Robertson has been appointed as Investment Advisor.
12. 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.
13. The performance of the managers is measured by independent external agencies.
14. 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.
15. 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.
16. The Fund’s Officers undertake the day to day monitoring of the investment of the Fund.
17. The Fund has a service plan that sets out in detail the development of the structure and processes that govern the investment of the Fund.



## Investment Objectives and Policy

18. 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.
19. In order to assist in setting the Fund's strategic investment policy, an asset liability modelling study is carried out. This study examines the Fund's financial position, the profile of its membership, the nature of its liabilities and includes an analysis of the expected ranges of outcomes from differing investment policies.
20. The current strategic asset allocation is based upon a study carried out as at 30th November 2004 by Hymans Robertson, based upon the liabilities shown by the 2004 valuation. The projected investment returns that were used in this study are shown in an appendix. Having considered the outcome of this initial study, the Committee concluded that a diversified portfolio, of which about 67.5% is invested in UK and overseas equities, 22.5% in bonds and 10% in property, represented a suitable strategic asset allocation benchmark for the Fund. The degree and nature of risks attaching to such a portfolio, when taken in conjunction with the expected returns, were considered by the Committee to be appropriate for the Fund.
21. An appendix is attached that sets out the detail of the strategic benchmark.
22. The Committee will continue to monitor the suitability of this policy in the light of the Fund's developing liabilities and finances.

## The 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, Corporate bonds and currencies.
26. Following consideration of the efficiency, liquidity and level of transaction costs likely to prevail within each market, the Committee determined that up to 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 by 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.
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 where it has been agreed with a manager that its use is inappropriate.
32. An appendix is attached that 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 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 liaising 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 investment 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 UK quoted companies should take account of the principles contained in the Combined Code and of the guidance offered by relevant organisations, including that contained in the Responsibilities of Institutional Shareholders and Agents - Statement of Principles, prepared by the Institutional Shareholders Committee in 2002. 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.
53. Investment of money purchase AVCs is undertaken through the Prudential Assurance Company. 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.

54. The Committee reviews the suitability of the AVC arrangements annually, or more frequently if required, based upon advice provided by Hewitt Bacon and Woodrow.

55. The Fund also has an AVC facility with Equitable Life. Due to Equitable's well publicised difficulties, this facility is no longer promoted by the Fund and does not receive new investment contributions.

### Compliance with Principles of Investment Practice

56. The Fund complies with all of the Principles of Investment Practice, as set out in the document called CIPFA Pensions Panel Principles for Investment Decision Making in the Local Government Pension Scheme.

### Limits on Investment in Partnerships

57. The Regulations contain the following limits on the percentage of a pension fund that may be invested into a partnership;

- 2% in respect of all contributions into any single partnership;
- 5% in respect of all contributions into partnerships.

58. The limits apply at the time that an investment is made.

59. The Regulations provide for the limits to be raised as follows, subject to certain requirements being met;

- 5% in respect of all contributions into any single partnership
- 15% in respect of all contributions into partnerships.

60. 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:

61. At its meeting on 7th June 2005, the Committee resolved that the limits applicable to the Fund be raised in order to accommodate the commitments that would be made in respect of this investment, as follows:

- The limit in respect of all contributions into any single partnership be raised from 2% to 2.5%.
- The limit in respect of all contributions into partnerships should be raised from 5% to 10%.

62. The Committee has taken proper advice in respect of this investment from the Investment Advisor, Hymans Robertson, and from the Fund's Officers.

63. This decision will apply for the period for which the Fund's strategic investment benchmark includes a 5% allocation to Private Equity, unless investment considerations require an earlier review.

64. No date has been set for an earlier review.

65. This decision is compliant with the Regulations.

## 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 update of the study carried out as at 30th November 2004.

Asset class	10 year median real return % pa
Global (ex UK) Equities (unhedged)	4.6
UK Equities	4.8
Property	2.9
AA Sterling long-dated Corporate Bonds	2.0
Long-dated UK Gilts	1.3
UK Index Linked Gilts	0.8
Foreign Bonds (unhedged)	2.0

The returns shown above were those projected from 30th November 2004 and hence would not necessarily apply at any subsequent date.

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.

Inflation has been assumed at 2.8%.

Strategic Benchmark		
Asset Class	Allocation	Index %
<b>UK Equities</b>	<b>27.50</b>	FTSE All Share
<b>Overseas Equities</b>	<b>40.00</b>	
- US	12.50	FTSE All World US
- Europe ex UK	13.50	FTSE World Europe ex UK
- Japan	7.00	FTSE All World Japan
- Other Far East	3.50	MSCI All Country Pacific Free ex Japan inc Malaysia
- Emerging Markets	3.50	MSCI Emerging Markets Free
<b>Fixed Interest</b>	<b>22.50</b>	
- UK Gilts	7.00	FTSE-A British Government All Stocks
- UK Index Linked	4.00	FTSE-A British Government Over 5 Year IL
- Sterling Non Government	9.00	ML Sterling Non Gilt All Stocks
- Overseas	2.50	JPM Global (non UK) Traded Bond Index, hedged into Sterling
<b>Property</b>	<b>10.00</b>	IPD Monthly Index

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.

## Management Structure

Manager	Mandate	Objective
Fidelity	UK Equities	To aim to outperform the FTSE All Share periods Index by + 1.5% p.a. over 3 year rolling with the return being no more than 4% below the Index in any one year.
UBS	Pan European Equities	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	To outperform the FTSE All World Index by 2% 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	To outperform the MSCI Emerging Markets Free Index.
Schroder	Japanese Equities	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.
Schroder	Pacific ex Japan Equities	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.
Legal and General	UK Equities	To match the return on the FTSE All Share Index.
Legal and General	US Equities	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	To match the return on the FTSE – A British Government Over 5 Years Index Linked Index.
Legal and General	AAA Fixed Interest	To match the return on the iBoxx Sterling AAA All Stocks Index.
Various	Private Equity	Notionally, 5% above the returns on quoted equity.
Prudential M&G	Corporate Bonds	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 Gilts 15% FTSE - A British Government All Stocks 5% FTSE – A British Government Over 5 Years Index Linked Index.
Henderson	Government Bonds	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 British Government Over 5 Years Index Linked Index. 25% Merrill Lynch Sterling Non Gilt All Stocks. 30% JP Morgan Global (Non UK) Traded Bond Index, hedged into Sterling.
Arlington Property Investors	Property	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  
on 7th June 2005

## 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.
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.

## 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.

## 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, including that contained in The Responsibilities of Institutional Shareholders and Agents – Statement of Principles, prepared by the Institutional Shareholders Committee in 2002.
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.



# Notes





## How to contact us

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Our information is available in other ways on request.

We can provide information in other languages, braille formats, large print.

We also have access to audio aids and BSL interpretation services.