



Teesside Pension Fund

Statement of Investment Principles

2010



Contents

1.	INTRODUCTION	3
2.	INVESTMENT RESPONSIBILITIES	3
3.	THE MYNERS PRINCIPLES	4
4.	TYPES OF INVESTMENTS TO BE HELD	6
5.	THE BALANCE BETWEEN DIFFERENT TYPES OF INVESTMENT	8
6.	RISK	9
7.	INVESTMENT OBJECTIVE	10
8.	THE REALISATION OF INVESMENTS	11
9.	INVESTMENT STRATEGY: ETHICAL, SOCIAL & ENVIRONMENTAL PERSPECTIVE	11
10.	SHAREHOLDER GOVERNANCE	11
11.	PERFORMANCE MEASUREMENT	12
12.	COMPLIANCE & MONITORING	12



1. Introduction

The Local Government Pension Scheme (Management and Investment of Funds) (Amendment) Regulations 1999 require that Local Government Pension Scheme administering authorities prepare, publish and maintain Statements of Investment Principles (SIP).

This is the Statement of Investment Principles (SIP) of the Teesside Pension Fund ("the Fund"), which is administered by Middlesbrough Council ("the Administering Authority").

It has been prepared by the Administering Authority in collaboration with the Fund's actuary and after consultation with the Fund's employers and investment advisers.

2. Investment Responsibilities

The **Teesside Pension Fund and Investment Panel** (The Investment Panel) has responsibility for:

- Preparing the Statement of Investment Principles,
- Monitoring compliance with the Statement and reviewing its contents periodically,
- Appointing investment managers, advisors and external service providers,
- Reviewing on a regular basis the investment manager's performance against agreed benchmarks and satisfying themselves as to the manager's expertise,
- Ensuring that the terms of the Management Agreement have been complied with,
- Reviewing on an annual basis the internal systems and controls in place to monitor compliance with the Management Agreement.

The **Director of Resources** is responsible for:

- Ensuring effective internal controls are in place,
- Overseeing the activity of the Head of Investments & Treasury Management and the Loans & Investment Section,
- Assisting the Investment Panel in the preparation and review of the SIP and ensuring compliance with its terms,
- Providing advice, after consultation with the Fund's Actuary, as to the maturity of the Scheme and its funding level in order to assist the Investment Panel in balancing the short term and long term objectives of the Fund.

The **Head of Investments & Treasury Management** is responsible for:

- The investment of Fund assets in compliance with prevailing legislation and the requirements of the Management Agreement,



- Implementing the Investment Advisor's recommendations on asset allocation within the parameters laid down,
- Security selection within asset classes,
- Preparation of quarterly reports to the Investment Panel and an annual report on investment performance,
- Reviewing investment management, custodial and other external relationships and advising the Investment Panel as to future policy with a view to delivering continuing improvements within a Best Value regime,
- Implementing the Investment Panel's policies on Shareholder Governance and Ethical, Social and Environmental Investment,
- Assisting the Director of Resources and the Investment Panel in the preparation of the SIP, its regular review and compliance.

The **Fund Custodian** is responsible for:

- Ensuring that the Fund's assets are secure and that the Fund is able in a timely fashion to meet its contractual obligations,
- Its own compliance with prevailing legislation,
- Providing the Investment Panel with quarterly valuations of the Fund's assets,
- Collection of all income due to the Fund,
- Carrying out the instructions received from the Head of Investments & Treasury Management in respect of voting actions,

The **Investment Advisors** are responsible for:

- Advising the Investment Panel on the most appropriate short term asset allocation for the Fund,
- Advising the Investment Panel on the most appropriate long term asset allocation for the Fund as part of the Asset/Liability Study,
- Advise the Investment Panel in the preparation and review of the SIP,
- Advise the Investment Panel in their regular monitoring of the performance of the investment managers.

3. The Myners Principles

The Myners Principles have been promoted by the Government as representing best practice for institutional investors. Compliance with the six "High Level" Principles was agreed by the Investment Panel on 10th June 2009. These Principles are supported by statutory guidance. The guidance contains examples of good practice, although not every element of the guidance is expected to be implemented, dependent on the circumstances of the particular fund.

PRINCIPLE 1: EFFECTIVE DECISION-MAKING



Trustees should ensure that decisions are taken by persons or organisations with the skills, knowledge, advice and resources necessary to take them effectively and monitor their implementation.

Trustees should have sufficient expertise to be able to evaluate and challenge the advice they receive, and manage conflicts of interest.

Full compliance

PRINCIPLE 2: CLEAR OBJECTIVES

Trustees should set out an overall investment objective for the Fund that takes account of the scheme's liabilities, the strength of the sponsor covenant, as well as the attitude to risk of both the trustees and the scheme sponsor, and clearly communicate these to advisors and investment managers.

Full compliance

PRINCIPLE 3: RISKS AND LIABILITIES

In setting and reviewing their investment strategy, trustees should take account of the form and structure of the Fund's liabilities. These include the strength of the sponsor covenant, the risk of sponsor default and longevity risk.

Full compliance

PRINCIPLE 4: PERFORMANCE ASSESSMENT

Trustees should arrange for the formal measurement of the performance of the investments, investment managers and advisors. Trustees should also periodically make a formal policy assessment of their own effectiveness as a decision-making body and report on this to scheme members.

Performance of the investment managers is undertaken annually and the position of the advisors, including an assessment of performance, is undertaken periodically. The last such review of advisors was carried out in 2009. The Fund does not have a mechanism for trustees to formally assess their own effectiveness and to report that assessment to scheme members.

PRINCIPLE 5: RESPONSIBLE OWNERSHIP



Trustees should adopt, or ensure that their investment managers adopt, the Institutional Shareholders' Committee Statement of Principles on the responsibilities of shareholders and agents. A statement of the scheme's policy on responsible ownership should be included in

the Statement of Investment Principles. Trustees should report periodically to members on the discharge of such responsibilities.

Full compliance

PRINCIPLE 6: TRANSPARENCY AND REPORTING

Trustees should act in a transparent manner, communicating with stakeholders on issues relating to their management of investments, its governance and risks, including performance against stated objectives. Trustees should provide regular communication to scheme members in the form they consider most appropriate.

Full compliance

4. Types Of Investments To Be Held

The following categories of investment have been approved as suitable for investing Teesside Pension Fund monies:

UK Equities

provide an equitable share in the assets and profits of public companies. Income is derived from dividends which, although variable in amount from year to year, have historically risen above the rise in inflation. Equities produce capital gains and losses as share prices reflect investors' expectations of the prospects of a specific company, sector or market.

Overseas Equities

are similar to UK Equities but allow greater diversification amongst industries and companies than would be available in UK quoted companies alone. They have exposure to the relationship between Sterling and the currency of the market where the share price is listed. Investment returns will be enhanced, or reduced, by fluctuations in that Exchange Rate. However, over the very long term, currencies are likely to reflect differentials in inflation rates and should, therefore, not affect returns on equities materially on such a time scale. Because of the likely excess return from equities (the so-called "Equity Risk Premia") a major proportion of the Fund's assets will probably be held in equities other than in exceptional economic or Fund-specific circumstances.

UK Bonds

are debt instruments issued by Governments and other borrowers. Bonds provide a fixed rate of interest and are generally redeemed at a fixed price on a known future date.



The price of Bonds primarily reflect the fixed level of interest, the period to redemption and the overall return demanded by investors. They are vulnerable to rising inflation and correspondingly benefit from falls in inflation.

Overseas Bonds

are similar to UK Bonds but have exposure to currency fluctuations. As with UK Bonds they are influenced by local inflation rates.

UK Index Linked Bonds

are bonds issued by Government and other borrowers. They provide interest and redemption value directly linked to a measure of inflation, usually the Retail Price Index, or a measure of change in some other Index. Index Linked Bonds may prove useful in matching some of the Fund's liabilities.

Overseas Index Linked Bonds

are similar to UK Index Linked Bonds but have exposure to currency fluctuations.

Property

is investment in land or buildings either directly by the Fund or indirectly through a pooled vehicle. Income comes from rents collected from tenants. Investment in property produces capital gains and losses as prices fluctuate in line with rental levels and investor demand. The contractual nature of rental agreements gives property some of the characteristics of bonds, whilst growth and inflation give it some of the characteristics of equities. It is, therefore, a useful diversifying asset class.

Derivative Instruments

such as Traded Options and Futures are mechanisms through which the Fund can be protected from sudden changes in share prices or Exchange Rates. Although not income producing they can produce capital gains and losses. They may be used conveniently to hedge the Fund's exposure to particular markets.

Alternative Investments

are investments in companies, which typically are not listed on a recognised Stock Exchange. Such investments can produce income in the form of dividends and can produce capital gains and losses. Because of the inherent lack of liquidity such investments should be expected to produce higher returns.

Exchange Traded Funds

are traded funds (ETF's) usually designed to track an index. They allow investment in specific areas such as commodities.

Pooled Investment Vehicles

such as Unit Trusts, Limited Partnerships, Open-Ended Investment Companies (OEIC's) and Insurance Funds are an alternative way of investing in shares, bonds and property to provide specialist management expertise and greater diversification. They may permit participation in venture capital and private equity, and also in infrastructure projects.

Cash

is invested in authorised institutions in accordance with the treasury management policy of Middlesbrough Council and will attract interest at market rates. Although it can be adversely affected by inflation, its nominal value remains constant, while that of other asset classes can be volatile.



Underwriting

the issue of shares by companies in which the Fund invests or wishes to invest, although not strictly an "investment" is

permitted within the constraints contained within the Management Agreement.

Securities Lending

the use of securities lending (also known as stock lending), was approved by the Investment Panel, within agreed limits. In practice the Fund has not entered into any securities lending arrangements due to concern about counterparty risk and it is not intended to do so without a further report back to the Investment Panel.

5. The Balance Between Different Types Of Investment

The LGPS Regulations require that administering authorities should "have regard to the need for diversification of investments" in order to reduce the risk of over concentration in one class of investment, which performs badly.

The Asset/Liability Study, carried out every 3 years, establishes a Benchmark asset mix against which actual Fund performance can be measured. It is recognised that the Teesside Fund is a UK based Fund with the majority of its liabilities in the UK. As part of this process a maximum/minimum range of % of the Fund to be held in the various categories of investment is determined and is reviewed as part of the Asset/Liability Study process.

The range of permitted investment in each asset class, expressed as a % of the Fund, currently agreed, is as follows:

	Max %	Min %
GROWTH ASSETS		
Global Equities	90	50
Property	15	5
Alternatives	10	0
PROTECTION ASSETS		
Bonds	25	5
Cash	15	0

As a result of the Asset/Liability Study the Investment Advisers and the Fund's Actuary recommend an asset mix designed to produce the long-term returns which the Fund requires to meet its future liabilities. On a quarterly basis the Advisors recommend a short-term strategy to suit current Market conditions. Once accepted by the Investment Panel implementation of that strategy is delegated to the Head of Investments & Treasury Management, or, in his absence, the Fund Manager.



6. Risk

There are three forms of risk:

- a) that associated with security of the Fund's assets;
- b) that associated with loss of value relating to those assets;
- c) that associated with the ability of those assets to provide required rates of return.

a) Security of the Fund's Assets

The Fund's Custodian, The Northern Trust Company, holds the majority of the Fund's Assets. An Agreement is in place protecting the Fund against fraudulent loss and regular checks are made by independent Auditors regarding the integrity of the Custodian's systems. In addition the Fund's Direct Property assets are registered in the name of Middlesbrough Council and the Title Deeds and documents held by the Fund's solicitors, Dechert. Cash balances belonging to the Fund are invested in accordance with agreed criteria, which take into account an appreciation of risk.

b) Asset Risk

The value of all investments can go down as well as up. Even investments in Gilts, securities issued by HM Government, are not without risk. Individual companies can cease to trade, with shareholders well down the list of creditors.

The best way to protect the Fund against asset risk is by diversifying into a number of asset classes, a range of countries and a range of companies. The Local Government Pension Scheme (LGPS) Regulations 1986 imposed certain limits on the proportion of the value of the Fund which could be invested in different types of investment. The LGPS (Management and Investment of Funds) Regulations 1998, revised in 2004, introduced changes to these limits, subject to certain conditions being met. The Investment Panel on 11 March 2004 decided that advantage should not be taken of the increased flexibility provided by the changes.

c) Investment Risk

One of the Trustees' most important duties is to make sure that the Fund has enough Assets to pay the benefits already earned by scheme members. On top of that they are looking to achieve sufficient return on those Assets to keep down the cost of building up future benefits.

In order to meet these responsibilities the Trustees set a performance benchmark against which they can measure the progress of the Fund's investments. Funds which outperform their benchmark can reduce costs compared with those Funds which under-perform.

For the Fund to significantly out-perform its benchmark it needs to have an Asset Mix which is different from that of its benchmark. The more out-performance is required the greater the differences will need to be. In other words out-performance cannot be achieved without taking risks.

Measurement of risk can identify whether the risk profile is, on one hand, large enough to deliver the required relative returns or alternatively so great as to lead to the possibility of serious underperformance.



The Teesside Pension Fund has an asset mix, which varies significantly from that of the Average Fund (as at 31 March 2010):

	Fund %	Average %
UK Equities	36	30
Overseas Equities	33	31
Bonds	13	22
Property	6	7
Cash	9	3
Alternatives	3	7
Total	100	100

The result of holding an asset mix, which differs significantly from that of the Average, is that investment performance returns can be volatile compared with those achieved by the Average Fund. This could result in periods of underperformance.

The Asset/Liability Study, carried out every three years by the Fund Actuary in conjunction with the Fund's Investment Advisors, assesses the degree of risk which the Fund needs to incorporate into its investment strategy, mainly expressed as the split between bonds and equities, in order to meet its liabilities and in particular to achieve the goal of employer contribution rates which are both low and stable.

The Fund's Funding Strategy Statement sets out the assumed real rate of return, that is the rate of return above the return on Government Index-linked bonds, on the various categories of investment:

	Return per annum %
UK Equities	3.0
Overseas Equities	3.0
Bonds	2.5
Property	3.5
Cash	1.0

7. Investment Objective

The Fund invests monies received which are not immediately required to pay benefits. The long-term objective of this "pool" of investments is to have sufficient money available to meet future liabilities, in the form of benefits to its members, and at the same time to minimise the contribution payable by the Scheme employers.

The Fund Actuary, as part of the triennial Valuation process, estimates the average annual rate of return which the Fund's investments would have to achieve, in the long term, in order to meet the Fund's liabilities. The triennial valuation includes a risk assessment in relation to the valuation of its



liabilities and assets and the chief finance officer will report to the committee if, at any time, there is reasonable doubt about the valuation.

8. The Realisation Of Investments

The majority of investments should be readily marketable, so that the proceeds of sale should be available within two weeks. It is recognised that certain categories of investment, typically Property and unquoted securities are more difficult to sell. The Fund's cash balances will be managed in such a way as to ensure that sufficient balances are available to meet foreseeable demands, including payments to beneficiaries and monies which may be required to meet investment needs.

9. Investment Strategy: Ethical, Social & Environmental Perspective

A report to the Investment Panel on 12 March 1999 established the Fund's position on Ethical, Social & Environmental investment and agreed revised Guidelines. As a responsible investor, the Teesside Pension Fund wishes to promote corporate social responsibility, good practice and improved company performance amongst all companies in which it invests. The Fund will therefore monitor investee companies to ensure they meet standards of best practice in relation to their key stakeholders. The Fund considers that the pursuit of such standards aligns the interests of Fund members and beneficiaries with those of society as a whole. In furtherance of this policy, the Fund will support standards of best practice on disclosure and management of corporate social responsibility issues by companies and will pursue constructive shareholder engagement with companies on these issues consistent with the Fund's fiduciary responsibilities.

The Fund will explicitly consider climate change risks and opportunities in the investment process and engage with companies in which we invest to ensure that they are minimising the risks and maximising the opportunities presented by climate change and climate policy.

The Fund has adopted the Institutional Shareholders' Committee Statement of Principles and members will agree and periodically review its implementation.

In accordance with this policy, the Fund will seek where necessary through its own efforts and in alliances with other investors to pursue these goals. To this end the Fund is an active member of the Local Authority Pension Fund Forum.

10. Shareholder Governance

The Fund believes that its role as shareholder requires it to exercise its voting rights in companies in which it invests. In furtherance of the policy the Investment Panel has agreed voting guidelines to enable the policy to be implemented. Following the appointment of PIRC as the Fund's service provider in 2008 revised guidelines were determined. These guidelines are available on the Fund's website www.teespen.org

The Fund's shareholder governance policy is restricted to the Fund's UK holdings.



11. Performance Measurement

Fund performance is measured by the independent performance measurers, the WM Company and reported to the Investment Panel annually. Although this compares the performance of the Fund against other Funds and the customised benchmark, the key measure of performance is against the Fund's liabilities. This methodology is used when carrying out the Asset/Liability Study.

12. Compliance & Monitoring

The Head of Investments & Treasury Management will submit a revised Statement to the Investment Panel when there has been a material change of policy or where circumstances require. Any interim changes necessary must be approved by the Investment Panel or, when circumstances dictate, by the Chair and will be incorporated in a revised Statement at the end of each year. The Statement is published on the Pension Fund website and copies are available, on request, to Scheme Members.

