

# Investment Valuation Procedures

This procedures manual sets out the specific guidelines used by Guardians management to enable the effective implementation of the principles contained in the Investment Valuation Policy **Kaupapa Here mō te Wāriu Haumitanga**.



**Procedures Owner:** General Manager Strategy & Shared Services

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## **Contents**

<b>Objective.....</b>	<b>3</b>
<b>Definitions .....</b>	<b>3</b>
<b>Scope.....</b>	<b>3</b>
<b>Responsibilities .....</b>	<b>4</b>
<b>Schedule 1: Valuation Methodology – additional processes.....</b>	<b>5</b>
<b>Schedule 2: Frequency of Valuations – additional processes.....</b>	<b>8</b>
<b>Schedule 3: Valuation Working Group – Terms of Reference .....</b>	<b>9</b>

## Objective

- 1.1 This document sets out additional information on procedures to be followed for the valuation of investments held by the NZ Super Fund and the Elevate Fund and should be read in conjunction with the *Investment Valuation Policy*.

## Definitions

- 2.1 To aid with interpretation of this document we have a Glossary of Terms, which defines all investment and technical terms used in our policies. In this procedure document the first instance of any such defined term is highlighted in **bold**. References to other documents are *italicised*.

## Scope

- 3.1 The Investment Valuation Policy and these Procedures set out the principles and procedures to be followed for the valuation of investments held by the NZ Super Fund and the Elevate Fund. They include requirements for valuation methodology, fair value hierarchy of valuation inputs and valuation frequency. These requirements apply to investments that are either managed internally or externally managed on behalf of the Guardians.
- 3.2 **Valuation methodology:** The valuation methodologies outlined in Schedule 1 of the Investment Valuation Policy and these Procedures will be applied to the NZ Super Fund's and the Elevate Fund's investments to determine fair value.
- 3.3 **Valuation frequency:** The frequency of investment valuations will be carried out in accordance with Schedule 2 of the Investment Valuation Policy and these Procedures, noting that:
  - 3.3.1 Capital flows (such as the provision of additional capital or the return of capital from an investment) will be reflected in the fair value of an investment immediately upon occurrence.
  - 3.3.2 Where there is evidence of impairment, fair value will be assessed immediately and if necessary, updated as soon as reasonably practicable. Evidence of impairment includes the financial difficulty of an investee entity, disappearance of an active market, obsolescence or damage as a result of environmental events.
  - 3.3.3 The VWG or the Audit & Risk Committee may request a review of the fair value of any investment at any time throughout the financial year.
- 3.4 **Valuation Working Group:** The VWG is an internal working group that is responsible for reviewing the valuation of investments in accordance with the *VWG Terms of Reference* outlined in Schedule 3. The VWG makes recommendations to management as to whether the investment valuations (including independent third party valuations) should be adopted and reports the results of their annual workplan, including the outcomes of their reviews, to the Audit & Risk Committee.
- 3.5 **Independent third party valuers:** Where an independent third party valuation is required, a suitable external valuer will be engaged based on an assessment of their qualifications, experience, capacity to undertake the work, reputation and independence from the Guardians.
- 3.6 **Consistency:** The methodology used for the valuation of investments will be applied consistently across all investments with similar characteristics, wherever practicable. It

will also be applied consistently across financial periods unless an alternative methodology becomes more appropriate.

## Responsibilities

<b>GM, Strategy and Shared Services</b> will:	<ul style="list-style-type: none"> <li>• ensure the Investment Valuation Policy and Procedures documents are kept current and fit for purpose</li> <li>• ensure the Investment Valuation Policy and Procedures are reviewed at least every five years</li> <li>• approve any alternative pricing sources for investments with observable/quoted market prices where the Custodian is unable to obtain a fair value</li> <li>• annually provide the Audit &amp; Risk Committee with a summary of individual investment valuations reviewed including the process followed, application of policy, key areas of focus and recommendations.</li> </ul>
<b>Chair of the Valuation Working Group</b> will:	<ul style="list-style-type: none"> <li>• ensure the VWG completes its annual workplan and discharges its responsibilities in accordance with the VWG Terms of Reference</li> </ul>
<b>Custodian</b> will:	<ul style="list-style-type: none"> <li>• act as valuation agent for the provision of fair value for certain investments</li> <li>• provide pricing guidelines to the Guardians and ensure a robust process is in place where a specific price or methodology is required by the Guardians for determining fair value</li> <li>• ensure their internal controls for the valuation of investments are reviewed on an annual basis by an independent auditor and provide the findings of that review to the Guardians</li> </ul>
<b>Lead Investment Professionals</b> will:	<ul style="list-style-type: none"> <li>• present investment valuations to the VWG for review in accordance with the Investment Valuation Policy and Procedures</li> <li>• prepare and review internal valuation models as required</li> <li>• advise the Investment Operations and Finance teams of any changes to an investment or the investment environment that may have an impact on fair value</li> <li>• assess third party independent valuers for suitability</li> <li>• act as the primary point of contact and liaise with third party independent valuers (or act as the primary point of contact for managers where third party independent valuers are not appointed directly by the Guardians)</li> </ul>
<b>Head of Risk</b> will:	<ul style="list-style-type: none"> <li>• report policy breaches immediately to the Risk Committee and Audit &amp; Risk Committee</li> </ul>

## Schedule 1: Valuation Methodology – additional processes

The table below outlines the valuation methodologies to be used for the main categories of the NZ Super Fund’s and the Elevate Fund’s investments

Investment category	Price sourced by Custodian	Valuation provided by manager/administrator	Cost or recent transaction	Third party independent valuation	Third party validation	Internal valuation
Investments with observable/quoted market prices	x					
Derivative financial instruments	x					
Collective investment vehicles		x				
Unlisted direct investments			x	x	x	x
Externally managed unlisted investments		x		x		

Source: *Investment Valuation Policy*

The following [procedures] supplement the information provided in “Schedule 1: Valuation Methodology” of the Investment Valuation Policy.

### Investments with observable/quoted market prices (NZ Super Fund only)

Investments with observable/quoted market prices include any investment that is listed on an exchange or forms part of an index. Examples include equities, fixed income securities, futures and options. For these instruments, fair value is obtained by our **Custodian** and determined with reference to quoted prices, using Level 1 inputs.

Where the Custodian is unable to obtain a valuation that is considered representative of fair value for an instrument, pricing will be obtained by the Guardians from an alternative source and communicated to the Custodian. Alternative pricing sources may be obtained from internal assessments or third parties such as brokers, counterparties or independent external valuers. These alternative pricing sources will be reviewed by the VWG and recommended for approval by the GM, Strategy and Shared Services. A schedule of all approved alternative pricing sources will be maintained by the Guardians.

### Derivative financial instruments (NZ Super Fund only)

Derivative financial instruments are investments where the value is derived from an underlying instrument. Fair value is obtained by our Custodian from independent, industry-recognised, pricing sources where possible, or via a manual pricing process, primarily utilising specified counterparty pricing, using Level 2 and/or Level 3 inputs.

## Collective investment vehicles (both NZ Super Fund and Elevate Fund)

**Collective investment vehicles** include investments in hedge funds, private equity investment funds and other pooled investment funds. They are valued based on the last price per unit (or other appropriate measure) of the investment as provided by the **investment manager** or administrator at valuation date. The price is based on the fair value of the underlying net assets or securities of the investment vehicle/fund. The fair value of the underlying net assets can be determined using a variety of methods including independent valuations, valuation models based on the price of recent transactions, earnings multiples, or discounted cash flows. The inputs used in determining fair value will be classified as Level 2 and/or Level 3 inputs as appropriate.

## Unlisted direct investments (NZ Super Fund only)

Unlisted **direct investments** include investments that are not listed on an exchange or do not form part of an index, are not collective investment vehicles and are not externally managed on behalf of the Guardians.

If cost, or the price observed from a recent transaction of an investment, is considered the best estimate of fair value, the relevant transaction must have occurred sufficiently close to the measurement date (within 1 year) and there shall be no evidence of any subsequent **material** change in value. In the context of the fair value hierarchy, this would constitute a Level 2 market-observable input. In the absence of a recent transaction providing a reliable estimate, the fair value of unlisted direct investments will be determined as follows:

Size of investment	Valuation Approach
=/ > 1% of NAV	Third-party independent valuation
0.5% - 1% of NAV	Third-party validation of internal valuation or third-party independent valuation
< 0.5% of NAV	Internal valuation or third-party independent valuation

*Source: Investment Valuation Policy*

Third party independent valuations will be mandatory for investments with fair values of greater than, or equal to 1% of the NZ Super Fund's NAV. These valuations will be reviewed in detail by appropriate investment professionals within the Guardians and presented to the VWG for review. If satisfied, the VWG will recommend adoption of the independent valuation.

Internal valuation models used for investments with fair values of greater than or equal to 0.5% and less than 1% of the NZ Super Fund's NAV will be reviewed by an independent third party who will validate the mechanics of the valuation model, confirm key variables and provide a reasonableness check of the output. A summary of the review will be presented to the VWG for review. If satisfied, the VWG will recommend the valuation be adopted.

Internal valuations of investments with fair values of less than 0.5% of the NZ Super Fund's NAV will be prepared using internal valuation models. These models will be prepared by personnel with appropriate knowledge and experience in conducting valuations and peer reviewed by a member of the investments team who is independent from the team responsible for managing the investment. A summary of the review will be presented to the VWG for review. If satisfied, the VWG will recommend the internal valuation be adopted.

Regardless of the thresholds contained in the table above, independent third party valuations may be obtained for any investment, irrespective of size, at the request of the investments team, the VWG or the Audit Committee if there are any other matters that may be considered **material**.

For all unlisted direct investments, irrespective of size, internal valuation models will be developed and regularly maintained by the Guardians' investments team as a reference point to inform the final valuation.

If the fair value of an investment is expected to move between the size categories outlined above (for example, the most recent valuation is less than 1% of the NZ Super Fund's NAV but its current fair value is expected to be above 1% of the NZ Super Fund's NAV, or vice versa), the valuation approach used will be that of the larger size category.

### **Externally managed unlisted investments (NZ Super Fund only)**

Externally managed unlisted investments comprise investments and co-investments that are externally managed on behalf of the Guardians, are not listed on an exchange or form part of an index and are not collective investment vehicles.

For investments with fair values of greater than or equal to 1% of the NZ Super Fund's NAV, fair value will be determined by independent third party valuation. These valuations will be reviewed in detail by appropriate investment professionals within the Guardians and presented to the VWG for review. If satisfied, the VWG will recommend adoption of the independent valuation.

For externally managed unlisted investments with a fair value of less than 1% of the NZ Super Fund's NAV, fair value will be provided by the external investment manager. That fair value will be based in turn on the fair value of the underlying net assets of the investment which is determined using a variety of methods including independent valuations, valuation models based on the price of recent transactions, earnings multiples or discounted cash flows.

Independent third party valuations may be obtained for any externally managed unlisted investment less than 1% of the NZ Super Fund's NAV at the request of the investments team, the VWG or the Audit Committee if necessary.

## Schedule 2: Frequency of Valuations – additional processes

The following procedures supplement the information provided in “Schedule 2: Frequency of Valuations” of the Investment Valuation Policy

The table below outlines the frequency of valuations for the main categories of the NZ Super Fund’s and the Elevate Fund’s investments.

Investment category	Minimum frequency of valuations			
	Daily	Monthly	Quarterly	Annually
Investments with observable/quoted market prices	x			
Derivative financial instruments		x		
Collective investment vehicles			x	
Unlisted direct investments				x
Externally managed unlisted investments				x

Source: *Investment Valuation Policy*

The fair value of investments with quoted market prices will be updated at least daily.

The valuation frequency for derivative financial instruments will vary depending on the specific instrument and the availability of data. The fair value of derivative financial instruments will be updated as frequently as possible (daily, in most cases) but reviewed monthly, to coincide with financial reporting cycles.

The fair value of collective investment vehicles will be updated based on the most recent quarterly statement received from the investment manager or administrator, noting that the timeframes for receiving these statements may vary, such that it is possible for a valuation to be up to six months old at balance date. This approach is in line with standard industry practice.

The fair value of unlisted direct investments and externally managed unlisted investments will be updated at least annually, to coincide with the end of financial year or when a material event occurs that warrants a revaluation of the asset. Where a material change in fair value has occurred during a financial year, the lead investment professionals will present an updated valuation to the VWG as soon as reasonably practicable.



## **Schedule 3: Valuation Working Group – Terms of Reference**

### **1. Purpose**

The purpose of the Valuation Working Group (VWG) is to review the valuation of investments held by the NZ Super Fund and the Elevate Fund as required by the Investment Valuation Policy. The VWG makes recommendations to management as to whether the investment valuations should be adopted and reports the results of its annual workplan, including the outcomes of their reviews, to the Audit & Risk Committee.

### **2. Membership**

Members of the VWG are:

- GM Strategy and Shared Services (Chair)
- Head of Finance
- Head of Direct Investment
- Head of Portfolio Investments
- Head of External Investment Partnerships

Subject matter experts may be invited to attend meetings of the VWG where the review of investments fall within their area of expertise. External experts may also be invited to attend meetings if required. A member of the Finance team will provide secretarial services.

A quorum for any meeting will be two members with at least one representative from the Finance team.

### **3. Responsibilities**

The VWG is responsible for ensuring that the valuations of the NZ Super Fund's and the Elevate Fund's investments adopted in the annual financial statements have been determined based on the valuation methodology and frequency as set out in the Investment Valuation Policy.

In particular, the VWG will:

- Review the pricing policies used by NZ Super Fund's custodian, Northern Trust and satisfy themselves they are fit for purpose;
- Obtain confirmation from the appropriate investment professionals that the valuations of collective investment vehicles as provided by external investment managers or administrators are appropriate;
- Review unlisted investments held at cost for evidence of impairment;
- In respect of independent third party valuations, ensure:
  - External valuers proposed for appointment have been assessed for suitability by the appropriate investment professionals within the Guardians, taking into account at a minimum qualifications, experience, capacity to undertake the work, reputation and independence.
  - External valuers are considered for rotation at least every 3 years.
  - External valuers prepare valuations in accordance with applicable financial reporting standards and any other legislative requirements as applicable.
- Review the valuations of unlisted investments and the assumptions therein to ensure they are fit for purpose;
- Make recommendations to management as to whether the investment valuations should be adopted or provide justification where independent third party valuations are not recommended for adoption;

- Report their findings to the Audit & Risk Committee. This report should include a summary of the individual valuations reviewed, the process followed, application of policy, key areas of focus and recommendations.

A risk-based or 'tiered' approach is applied when determining the level of review for the valuations of unlisted investments.

The VWG should consider whether there have been any events or changes in assumptions that would justify a departure from an independent third party valuation. Consideration should be given to:

- Significant changes in market conditions;
- New information that would have a material impact on valuation;
- Changes in probability weightings, if appropriate, due to changes in facts and circumstances.

#### **4. Meetings**

The Group will meet at least quarterly.