



PENSIONS COMMITTEE 12 November 2020

Subject Heading:

**SERVICE REVIEW OF THE PENSION
FUND CUSTODIAN**

SLT Lead:

**1 October 2019 to 30 September 2020
Jane West**

Report Author and contact details:

Debbie Ford
Pension Fund Manager (Finance)
01708432569

Policy context:

Debbie.ford@onesource.co.uk

Services are reviewed to ensure that the Pension Fund is receiving best value for money and is benefiting from all the services the custodian has to offer

Financial summary:

Costs for the custodial services for the period are met by the Pension Fund

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[X]
Places making Havering	[X]
Opportunities making Havering	[X]
Connections making Havering	[X]

SUMMARY

This report reviews the performance of the Custodian, State Street, for the period 1 October 2019 to 30 September 2020.

RECOMMENDATIONS

It is recommended that the Committee notes the views of officers on the performance of the Custodian and makes any comment on the report which it considers appropriate (Table 1 and Section 3 refers).

REPORT DETAIL

1. Background

- 1.1 Custodial services were formerly delivered by State Street which was terminated with effect from 30 September 2019. State Street were not looking to retain Local Government Pension Scheme (LGPS) clients as it was no longer suitable for their business model.
- 1.2 A new custodian (Northern Trust) was appointed to commence Custodial and Performance measurement Services from 1 October 2019. The Pension Funds within oneSource and the London CIV (LCIV) now share the same custodian. Using a single provider across the LCIV and with other underlying LGPS will benefit from having opportunities for efficiencies e.g. having a single system for the transition process, cost benefits (economies of scale from the full breadth of the LCIV relationship) and reduced operational risk.
- 1.3 Contract duration is 4 years and expires on the 31 September 2023. This initial contract length only covers 4 years so that an assessment can be made as to how custodial services will be delivered in the future and how monitoring services may be provided by LCIV.
- 1.4 This period of review covers the custodial and performance measuring services delivered by Northern Trust only.

2. Review of the Custodian's performance

- 2.1 The Custodian operate a wide range of functions. This falls into the following main categories:
 - Safe Keeping and Custody of assets
 - Investment Accounting and Reporting.
 - Performance Measurement

2.1 (a) Safe Keeping and Custody

This refers to the maintenance of accurate records and certificates of the ownership of stock and ensuring that dividend income and other distributions are received appropriately. The Custodian also manages the tax position of the pension fund (the 'Fund'), claiming back any recoverable overseas withholding tax paid on dividends received and maintaining the tax records of the fund.

2.1 (b) Investment Accounting and Reporting

The Custodians produce accounting reports that are used for producing the Pension Fund Statement of accounts and enable us to comply with the International Financial Reporting Standards (IFRS) and CIPFA accounting guidance. These reports are accessed and downloaded from their client portal "passport".

They keep a record of the book costs (valuations) and the holdings in the various asset classes for each of the investment managers' portfolio as well as at the total fund level.

The custodian contract also includes completion of the relevant investment sections of the UK Office of National Statistic Returns (ONS) which is a statutory requirement.

2.1 (c) Performance measurement

This is a key part of the investment management process and forms an essential component of the reporting requirements of the Fund. Performance measurement enables the Pensions Committee and officers to understand whether the investment objectives of the Fund are being met and if the fund managers are achieving their targets. To enable the Fund to do this Northern Trust produce monthly and quarterly reports setting out rates of return versus benchmarks for each manager and the whole fund over a number of time periods extending from one month to inception.

- 2.2 Services are reviewed annually to ensure that the Fund is receiving best value for money and is benefiting from all the services the custodian has to offer. Monitoring the contract also meets post contract award procedures and ensures services are being delivered in accordance to the contract.
- 2.3 Officers have assessed the service against a set of criteria and Officers have shared the outcome of the service review with Northern Trust, which has been set out in the following table:

Table 1

CRITERIA	ASSESSMENT
Safe Keeping and Custody of Assets	
It is important that the Pensions Committee and officers have confidence that all assets are secure and have been properly accounted for.	<p>Officers review the custodians audited System and Organisation Control (SOC1) report produced annually. No concerns were raised in their latest report covering the 12 months to 31 Sept 2019. The Sept 20 report will not be available until approximately 6 months after the period end date.</p> <p><i>Officers have confidence that the assets are accounted for correctly.</i></p>
Investment Accounting and Reporting	
It is important that accurate accounting records are maintained and appropriate reconciliations are able to be made against the fund's investment managers records.	<p>Officers run detailed reports from the custodian's website using their "passport" tool. These reports are reconciled to the fund manager reports and any differences are investigated. This provides assurances that accurate records are being maintained.</p> <p><i>Officers are satisfied that accurate accounting records are maintained and acknowledge the effort to ensure the smooth transition of assets from the former custodian.</i></p>
Prompt and responsive service	<p>Invoice issuance has not been prompt. Invoices have been received for the three quarters from 1 October to 30 June 20 and these were not received until late June 20. Officers have yet to obtain familiarity with the contents of the invoices and following initial enquires the invoices were reissued in September 2020.</p> <p><i>Officers have yet to review the revised invoices to ensure costs have been applied in line with agreed contract price.</i></p>
Good communication and support	Officers communicate frequently with

CRITERIA	ASSESSMENT
	<p>the custodian covering general day to day operations and to obtain assistance in ensuring investment instructions templates are completed correctly.</p> <p>Training and support was provided to officers in running reports from their website.</p> <p>Regular catch up meetings are held between the Custodians client officers and Havering officers.</p> <p>The Custodian continues to facilitate home working and there has been no service disruptions as a result of working restrictions introduced during COVID-19 lockdown and thereafter.</p> <p><i>Communications and support continue to be satisfactory.</i></p>
<p>Provision of data for the Office of National Statistics (ONS) Returns</p>	<p>New templates were introduced by ONS commencing with Quarter ending June 2019. The Fund uses the ONS service provided by the custodian and they complete the investment sections within the return and answer/resolve any queries raised by ONS. These have been completed within the required timescale.</p> <p><i>Officers are satisfied with this service.</i></p>
<p>Performance Measurement</p>	
<p>It is important that the Pensions Committee and officers understand whether the investment objectives of the Fund are being met and if the fund managers are achieving their targets.</p>	<p>To enable the fund to do this Northern Trust produce monthly and quarterly reports setting out rates of return versus benchmarks for each manager and the whole fund over a number of time periods that cover 1 month, 3 months, 1 year, 3 years, 5 years and inception. Performance reports are available via the custodian's website using the "RADAR" tool.</p>

CRITERIA	ASSESSMENT
	<p><i>Officers are appreciative of the work carried out to ensure the historical performance data was captured when assets were transitioned from the former custodian.</i></p> <p><i>Monthly performance reports are received in a timely manner.</i></p>

3. Conclusion

- 3.1 This is the first year of operation of custodial services with Northern Trust and officers acknowledge the efforts by all to ensure a smooth transition from the former custodian.
- 3.2 Officers are satisfied with the provision of safe keeping and custody functions.
- 3.3 Officers are satisfied with the overall investment accounting and reporting functions.
- 3.4 Officers are satisfied with the performance monitoring service.

IMPLICATIONS AND RISKS

Financial implications and risks:

The Fund's asset pool provider LCIV use Northern Trust as their appointed custodian and as a result offered a reduced pricing structure for those funds that have assets invested on the LCIV platform.

The costs for custody contract cover transaction charges, administration costs, Foreign exchange charges, ONS submissions and performance measurement costs.

Custody fees are based on a unit price applied to the value of the individual fund's asset values and each transaction.

ONS charges to be applied in line with agreed contract price.

Pensions Committee, 12 November 2020

Performance Measurement fees will be charged based on the agreed contract price and include costs for accessing each unique index family.

Invoices have only been received for the three quarters from 1 October to 30 June 20 and these were not received until late June 20. Following initial enquires the invoices were reissued in September 2020. Officers have yet to review the revised invoices to ensure costs have been applied in line with agreed contract price and based on invoices received (unchecked), the costs to June are £39,282 and estimated to £52,375 for the last quarter to Sept) (prior year 1 Oct 18 – 30 Sep 19 £48,875) See table below for fee breakdown:

Fee Breakdown	Oct 19 to Sept 20	Oct 18 to Sept 19
	Estimated	Actual
	£	£
Custody Fee	29,397	28,307
Performance Fees	22,978	20,568
Total	52,375	48,875

Foreign exchange costs are the main attribution for an increase in costs compared to prior year and officers will discuss with the custodian a more cost efficient way of handling the foreign exchange transactions.

The custodian and performance measurement fees are met from the Pension Fund.

There is a risk that the Fund's value could be misstated if poor or incorrect data was provided by the custodian. This is mitigated by frequent reconciliations by the custodian to fund manager records and officer reconciliations. Accounting and reporting information is critical for year-end processes and these need to be produced in a timely manner to ensure accounts can be closed within statutory timeframes.

Officers also carry out reviews of Northern Trust Internal Control reports issued by their external auditor. These reports detail tests undertaken by the auditors, testing their internal control environments and key procedures. No material internal control issues were reported.

Legal implications and risks:

There are no apparent legal implications or risks arising from this report.

Human Resources implications and risks:

The recommendations made in this report do not give rise to any identifiable HR risks or implications that would affect either the Council or its workforce.

Equalities implications and risks:

Pensions Committee, 12 November 2020

The Public Sector Equality Duty (PSED) under section 149 of the Equality Act 2010 requires the Council, when exercising its functions, to have due regard to:

- i. the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;
- ii. the need to advance equality of opportunity between persons who share protected characteristics and those who do not, and;
- iii. foster good relations between those who have protected characteristics and those who do not.

Note: 'Protected characteristics' are: age, sex, race, disability, sexual orientation, marriage and civil partnerships, religion or belief, pregnancy and maternity and gender reassignment/identity.

The Council is committed to all of the above in the provision, procurement and commissioning of its services, and the employment of its workforce. In addition, the Council is also committed to improving the quality of life and wellbeing for all Havering residents in respect of socio-economics and health determinants

An EqEIA is not considered necessary regarding this matter as the protected groups are not directly or indirectly affected.

BACKGROUND PAPERS

None