



Havering
LONDON BOROUGH

PENSIONS COMMITTEE 21 March 2023

Subject Heading:

**SERVICE REVIEW OF THE PENSION
FUND CUSTODIAN**

CLT Lead:

**1 October 2021 to 30 September 2022
Dave McNamara**

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Policy context:

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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, Northern Trust, for the period 1 October 2021 to 30 September 2022.

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 Northern Trust was appointed to commence Custodial and Performance Measurement Services from 1 October 2019 and expires on the 30 September 2023.
- 1.2 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 Officers are in the process of renewing this contract. As with the previous contract award, it is envisaged that this will be a direct award given that Northern Trust already have the market share of the London Funds (23 out of 32) and there are limited providers in the market (subject to governance decision making process).
- 1.4 This period of review covers the custodial and performance measuring services delivered by Northern Trust.

2. Review of the Custodian's performance

- 2.1 The Custodian operate a wide range of functions. This falls into the following main categories:

(a) Safe Keeping and Custody of assets

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.

(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.

(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 for 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 adopted the RAG rating method to define Green (Favourable output), Amber (Neutral, may require further monitoring) Red (Unfavourable). 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	Rating
Safe Keeping and Custody of Assets		
It is important that the Pensions Committee and officers have confidence	Officers review the custodians audited System and Organisation Control	GREEN: Officers have confidence that the assets are

CRITERIA	ASSESSMENT	Rating
that all assets are secure and properly accounted for.	(SOC1) report produced annually. No concerns were raised in their latest report covering the 12 months to 30 Sept 2021. The Sept 22 report will not be available until approximately 6 months after the period end date.	accounted for correctly.
Investment Accounting and Reporting		
It is important that accurate accounting records are maintained and appropriate reconciliations can be made against the Fund's investment managers records.	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 investigated. This provides assurances that accurate records are maintained. Access to additional reporting functionality further assisted officers in reconciling the 2021/22 accounts.	GREEN: Officers are satisfied that accurate accounting records are maintained with no audit issues identified to date.
Prompt and responsive service	Reponses to queries are dealt with promptly.	GREEN: Officers are very satisfied and appreciative of the responsive service
Good communication and support	Officers communicate frequently with the custodian covering general day-to-day operations and to obtain assistance in ensuring investment instructions templates are completed correctly.	GREEN: Communications and support continue to be very satisfactory.
Provision of data for the Office of National Statistics (ONS) Returns	The Fund uses the custodians ONS service and they complete the investment sections within the return and answer/resolve any queries raised by ONS. These have	GREEN: Officers are very satisfied with this service

CRITERIA	ASSESSMENT	Rating
	been completed within the required timescales.	
Performance Measurement		
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.	Northern Trust performance measurement service produce monthly and quarterly reports setting out returns 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.	GREEN <i>Performance reports are received within specified timescales and officers are very satisfied with this service.</i>

3. Conclusion

- 3.1 Officers are satisfied with the provision of safekeeping 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:

As the Fund's asset pool provider London CIV use Northern Trust as their appointed custodian the Fund benefits from a reduced pricing structure offered for those funds that have assets invested on the London CIV platform.

Upon reviewing reconciliation and year-end processes, management recognised the potential key person risk for reconciling the accounts and decided, for service planning reasons, to expand the current contract to include the custodian's additional Specialist accounting reporting service. This additional service means that the custodian is able to produce the accounts and provide officers with access to the

comprehensive suite of financial reports, which will further support the reconciliations of the accounts. Officers used this facility for the first time whilst closing the 2020/21 statement of accounts and found this very useful in providing assurance that in-house reconciliations undertaken during the year were accurate

This additional accounting service cost of £10,013 p.a. is reflected in table 2 below.

See fee table below for fee breakdown:

Table 2

Fee Breakdown	Oct 19 to Sept 20	Oct 20 to Sept 21	Oct 21 to Sept 22	Total
	Actual £	Actual £	Actual £	Actual £
Custody Fee	29,085	26,127	31,144	86,356
Accounting Services	0	5,000*	10,013	15,013
Performance Measurement Fees	23,110	23,849	26,947	73,906
Total	52,195	54,976	68,104	175,275

* part year only – this service commenced 1 April 2021

Custody – fees cover transaction charges, administration costs, foreign exchange charges and data for use in ONS submissions.

Accounting Services – production of reports used for producing the Pension Fund Statement of Accounts. This additional service was procured from 1 April 2021

Performance Measurement - fees are applied against each manager's performance data and the index against which it is measured.

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.

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

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:

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