

Pensions Audit Sub-Committee

10am, Monday, 16 December 2013

Global Custody Services Performance

Item number	5.4
Report number	
Wards	All

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Executive summary

Global Custody Services Performance

Summary

This report presents the Key Performance Indicator Report for the 6 Months ended 30 September 2013 provided by Northern Trust. The purpose of this report is to demonstrate that the performance of the custodian is regularly monitored to ensure that the services provided meet the needs of the three Pension Funds.

The conclusion is that Northern Trust's services are meeting the needs of the three Pension Funds and are of a high standard.

Recommendations

Pensions Audit Sub-Committee is asked to note this report on the performance of the global custody service provided by Northern Trust.

Measures of success

Performance is measured against the indicators that have been set for the main services provided by Northern Trust.

Financial impact

The budget set for the provision of custody services for 2013/14 is £402k. This report has no impact on the cost of custody provision.

Poor performance of the custodian could have a financial impact on the three Pension Funds. For example: from delays in or failure to collect investment income or failure in the system to notify companies of decisions made in response to corporate actions. However, staff monitor service provision and corrective action would be taken if any issues were ever to arise.

Equalities impact

There are no equalities impacts arising from this report.

Sustainability impact

There are no sustainability impacts arising from this report.

Consultation and engagement

The Consultative Panel for the Lothian Pension Funds, comprising employer and member representatives, is integral to governance.

Background reading / external references

None

Global Custody Services Performance

1. Background

- 1.1 Following a competitive tender process, Northern Trust has provided investment custody services since early in 2011 for the three Pension Funds. Provision of these services is vital to the management of the Funds' investments. The range of services includes:
- Proving investment valuations and accounts.
 - Ensuring that investment transactions are processed within market requirements.
 - Collecting investment income.
 - Providing notification of all corporate actions and passing responses to the companies concerned.
- 1.2 In order to assess the services provided a number of key performance indicators have been agreed with Northern Trust. These indicators are subject of a report from Northern Trust, the latest of which is for the six months ended 30 September 2013. This is the first time that a report on custody services has been considered by Committee.

2. Main report

- 2.1 Page 2 of the appendix provides a summary of the status of the various performance indicators. In order to get a high level picture of performance the traffic light system is used. All of the performance indicators are on green with the exception of the one for corporate actions which is amber.
- 2.2 Information about all of the performance indicators is summarised below:

Month End Valuation Reporting

Description of Indicator	Month end valuation reports of investments completed and reviewed by Northern Trust and available to client within the target number of business days of end of the previous month.
Performance Traffic Lights	Green – Completed by business day 14 Amber – Completed by business day 15 Red – Completed by business day 16 or later
Service Rating	Green

Over Last Six Months to 30/9/13	Work completed by business day 14 for months April to September of 2013.
Comments	<p>Unreviewed valuations are available on business day one; these are accurate for quoted investments. Portfolios that contain unquoted investments take longer for valuation information to be obtained.</p> <p>Month end valuations provided by Northern Trust are reconciled in terms investment holdings with records maintained by the external or internal investment manager. In addition, checks are made on the prices used by Northern Trust and the prices used by the external or internal investment manager.</p>

Financial Reporting

Description of Indicator	<p>Since April 2012 Northern Trust has been responsible for providing investment accounts for all three Pension Funds. This includes a month end trial balance and summary accounts and at the year end additional information for inclusion in the annual accounts.</p> <p>Month end investment accounting packs should be completed and sent to client within the target number of business days of end of the previous month.</p>
Performance Traffic Lights	<p>Green – Completed by business day 18</p> <p>Amber – Completed by business day 19</p> <p>Red – Completed by business day 20 or later</p>
Service Rating Over Last Six Months to 30/9/13	<p>Green</p> <p>Work completed by business day 18 for months April to September of 2013.</p>
Comments	<p>More time is allowed at the year end for the preparation of the additional information required for the annual accounts.</p> <p>The month end accounts are checked by the Fund for accuracy.</p>

Trade Settlement Statistics

<p>Description of Indicator</p>	<p>Each investment market around the world has a set of requirements that must be followed regarding the settlement of trades (purchases and sales). These requirements include a fixed number of business days for a trade to be settled. For example, shares trade in the UK must be settled in a three day period. Within that period each side must “deliver” either the shares or the funds as appropriate.</p> <p>The indicator is the percentage of trades that have settled on time.</p>
<p>Performance Traffic Lights</p>	<p>Green – 94% or higher Amber – 92% to 94% Red – 91% or lower</p>
<p>Service Rating Over Last Six Months to 30/9/13</p>	<p>Green 96.69%</p>
<p>Comments</p>	<p>During the period there were a total of 3,806 trades of which 3,680 (96.69%) were settled on time. Of the 126 trades settled late, 114 were purchases and 12 were sales. This reflects the main reason for late settlement that Lothian Pension fund experiences – that the selling broker does not initially have sufficient shares to settle the purchase trade.</p> <p>Northern Trust provides a range of reports on settlement statistics (see below) this includes one that provides information by broker. This is particularly useful for identifying the source of settlement problems.</p> <p>Northern Trust provides contractual settlement on all trades. So in the case of sale trades, Northern Trust will credit the Fund with the cash proceeds on the contractual settlement date of the underlying trade regardless of whether it settles on time in the market. Northern Trust would then seek compensation by issuing a market claim against the purchasing broker.</p>

Income Collection Statistics

Description of Indicator	<p>It is the responsibility of the custodian to account for all dividend income when it becomes due and to receive the money into the bank when the dividend is actually paid.</p> <p>The indicator is the percentage of the number of income payments received on pay day.</p>
Performance Traffic Lights	<p>Green – 95% to 100%</p> <p>Amber – 90% to 95%</p> <p>Red – 90% or lower</p>
Service Rating Over Last Six Months to 30/9/13	<p>Green</p> <p>98.16%</p>
Comments	<p>The performance indicator is based on the number of income collections rather than their value. During the period there were a total of 1,846 income collections, 1,812 (98.16%) of which were received on the correct pay day.</p> <p>During the period the value of income collections was £56.9m, £56.0m (98.48%) of which was received on time – slightly higher than the statistic based on numbers.</p> <p>Northern Trust provides a range of reports on income receipts (see below) this includes one that provides information by country. This report would be useful to identify any problems at the market rather than individual company level.</p> <p>Northern Trust provides contractual income in 38 countries. This means that Northern Trust endeavours to credit the Fund's bank account with the income on its pay date irrespective of the actual date of receipt.</p>

Corporate Actions

<p>Description of Indicator</p>	<p>Corporate actions are events announced by companies that give shareholders the opportunity to make a decision on two or more potential choices. For example:</p> <ul style="list-style-type: none"> • Rights issue to buy additional shares • Dividend reinvestment in additional shares • Receive dividend in GBP, USD or EUR <p>It is the responsibility of the custodian to collate responses from its clients to corporate actions and communicate the results to the company. The Fund has the responsibility of responding to corporate actions on a timely basis.</p> <p>The indicator is the percentage of responses made by the client with the deadline date set by the company for a response.</p> <p>The Fund has the responsibility of responding to corporate actions on a timely basis.</p>
<p>Performance Traffic Lights</p>	<p>Green – 100%</p> <p>Amber – 95% to 99%</p> <p>Red – 94% or lower</p>
<p>Service Rating Over Last Six Months to 30/9/13</p>	<p>Amber</p> <p>95.13%</p> <p>But see comments below about potential falsely recorded late responses.</p>
<p>Comments</p>	<p>During the period there were 308 corporate actions, 293 (95.13%) of which are recorded as having been responded to within the time limit.</p> <p>Northern Trust provide an online system to advise clients of all upcoming corporate actions for the investments that are held. The same system is used by the client to record decisions. As the deadline for an action approaches and no response has yet been recorded, Northern Trust staff will attempt to contact the client for a response. Contact is</p>

	<p>initially made by e-mail and on the day prior to the deadline contact by phone is attempted. In the event that a client response cannot be obtained Northern Trust will elect the default option for the action.</p> <p>Northern Trust have advised that there is an issue with the accuracy of their report in that there are potentially a number of false late responses for those actions where Northern Trust staff had chased for a response via the phone / e-mail and had been given a response that was not recorded on their system in time. In such a situation the company will have had the response in time but the statistics are not recording this. It is understood that Northern Trust hope to resolve this problem in time for the next report.</p>
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3. Recommendations

- 3.1 Pensions Audit Sub-Committee is asked to note this report on the performance of the global custody service provided by Northern Trust.

Alastair Maclean

Director of Corporate Governance

Links

Coalition pledges

Council outcomes CO26 – The Council engages with stakeholders and works in partnerships to improve services and deliver agreed objectives.

Single Outcome Agreement

Appendices None