

Solving the outsourced fund administration problem

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The need for new investment products:

Today's investment professional who deals in specialty financial products faces a problem. Non-retail investors (such as high net worth individuals, corporations, or foundations) are constantly looking for new ways to improve their return while managing their risk. In order to satisfy these customers, the investment manager must constantly seek new market opportunities in order to satisfy their customers demand for improved financial performance.

In order to satisfy this demand, the investment manager can create a new financial product to package specific underlying investments in a target investment area. This packaging is typically in the form of a "fund" (or family of funds), that allows investors to pool their assets, paying the investment manager to invest according to the definition of the new product, with an expectation of returns according to the new funds definition. The fund definition specifies the target investment area, and typically has a set of target parameters which define the type of risk/return ratios the investor can expect. The investment manager will then market this new fund to investors.

The new product brings new complexity

These fund products are becoming increasingly diverse and complex in terms of their underlying holdings. The investment manager has his hands full, focusing his full attention on managing the dynamics of:

- cash flow into the fund from contributions;
- deciding which underlying investments to purchase and when,
- tracking the value of underlying investments (pricing, with differing time frames and availability)
- Tracking cash flow into and out of the fund from income and expenses associated with the underlying investments.
- Managing sufficient liquidity to return cash flow to investor when they decide to redeem shares.

The investment manager needs to get paid

In order for the Investment Manager to get paid for his work, funds have a wide variety of options about how to do it:

- A significant variety of fee structures (share classes with daily accruals, average daily balance for an account or set of accounts, contribution/redemption fees)

- Fees can be taken out as expenses of the fund (thus lowering price and performance), or taken by an explicit sale of participant units (which doesn't affect the price)

Whichever approach is taken, the mechanics of calculating fees needs to be handled accurately, automatically, and with fairness to all investors.

The investor needs a simple business process and information as well as a return

The investor needs a simple business process to make contributions and redeem shares. They need confirmation of their trades. They need to have detailed records about their activity with the fund (contributions and redemptions). They need performance data of their investments, compared with industry benchmarks. Depending on the type of fund and investor, they may also need to report detailed allocations of different types of income and expense for tax reporting purposes. They need simple access to this data, ideally in electronic format over a secure web connection.

The problem then becomes *how to keep the books*, give investors an exact accounting of their investment, make sure investment managers receive what they deserve, and keep investment business processes efficient.

New technology platforms are offloading record keeping details from investment managers.

There are new fund administration platforms available on the market today that solve the problems outlined above. These new platforms take care of the mechanics of investor trading, settlement of contribution and redemption cash transactions, unit record keeping, fund pricing, and the allocation of income, expense and management fees to participants. They come with an inventory of off the shelf reports, including trade confirmations, shareholder balances, month end, and income allocation reports.

Providing flexible “snap-in” customization

Some of these platforms have been architected to allow flexible customization. Because there are so many different options (fund structure, pricing, fee algorithms, custom reports), these platforms are designed to allow modular or “snap in” capability of new functionality, without starting over from scratch for each fund. More modern development tools allow for faster development of new functionality, helping investment managers to get their product to market faster.

Built using native web technology, with advantages for all parties

These newer systems are built from the ground up using web technology, which offers numerous and immediate advantages both to investors and investment managers.

Web based applications allow the user to bring up their application in a browser, and interact with the system as though the program was running on their local computer. The company does not have to maintain the system itself. The outsourced provider manages the release of new functionality, and backs up the system and underlying database. The security of both the system and the data is managed for the Investment Manager.

Flexible user access to centralized fund data

Web based applications also allow centralized access to the data associated with the fund. With the proper user security of newer systems, you can have different types of users receive customized views of the underlying system. Some may have full administrator access (creating and modifying the behavior of funds), or operator access (allowing for trading activity, setting up new participants and accounts, calculate new unit prices, and automatically distribute month end reports), or simply “spectators”, who can see reports and graphs, but not change any of the underlying data. This flexible architecture leaves the Investment Manager with options about whether to outsource some, or all of the operations support effort.

These platforms can also provide flexible branding, which keeps the investor from even knowing that the outsourced record keeper even exists.

Independence of administration helps with compliance and audits

There is another benefit in outsourcing the fund administration. By having an independent and objective party manage the mathematics of the fund, the Investment Manager can present a more auditable, and independent set of calculation, which helps to keep things clean in the days of changing regulations. It will also provide more confidence to investors, that there is a separate organization whose sole purpose is to make sure that business processes and transactions are executed to a common, documented standard.

Summary

The investment manager’s hands are full. His or her expertise is in making decisions about where investment should go, and focusing on the type of return promised to the investors. Supported by an outsourced record keeper, the Investment Manager can provide an excellent investing experience for their customer, and let them focus on what they do best....making investment decisions.

Who is Capnetix?

Capnetix helps investment managers stay focused on their investment decision making, by taking care of their fund administration bookkeeping. Capnetix provides a state of the art, configurable web based administration platform and administration services.

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