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## What Is Next For Expense Processing?

### ExpertView

By Paul Soltis



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Every industry has its Achilles' heel. For fund administrators, it's issues with data integrity and the lack of automation of key operations, such as expense processing. In terms of fund expenses, there is more to think about than advisor fee justification and distribution fee compliance. There are other problems that are potentially worse under the surface.

A recent survey by **Confluence** asked fund industry professionals "what is the one back-office challenge that concerns them the most on a daily basis?" The top answers: 29% reported lack of automation of key operations and 24% identified data integrity issues.

The fund administration business processes massive amounts of data every day. To minimize risk, increase efficiency, control costs and eliminate redundant calculations, data automation is essential. We've already seen progress in the automation of financial and performance reporting. The Confluence survey found that 67% of respondents indicated the back office operation for performance reporting was already automated, while 61% indicated the same for financial reporting.

While financial and performance reporting operations are well en route to benefiting from data automation, the area of expense processing lags well behind. The good news is 23% of respondents reported they have plans to automate this operation in the next 12-24 months.

As fund administrators continue to process expenses manually they suffer an unnecessarily high rate of error. Net Asset Value errors are the most serious and have the most negative impact. Other negative results of manual expense processing errors include a restated prospectus, fluctuating expense ratios, fluctuating yields, and budget variances. All require an explanation for the fund

Treasurer, the fund Board, the fund's auditor, and perhaps even to regulators. These difficult communications fall on the shoulders of the fund administrator.

Given the combination of a lack of automation and the potential for severe consequences resulting from errors, it's hard to believe a majority of fund administrators still process expenses manually in spreadsheets. According to **Ray Panko**, a professor of IT management at the University of Hawaii who conducted a 2008 analysis, close to 90% of spreadsheet documents contain errors.

A fund administrator's accounts payable process would benefit from a centrally managed book of payment events. With this, they will be able to automatically generate comprehensive forecasts per service or fund. By eliminating spreadsheets, fund administrators gain control over vendor data, such as wire instructions, and the data that feeds into the payment and budgeting processes. Multiple invoices and payers—including funds, sub-funds and non-fund entities—can be consolidated. The allocation of expenses across funds and sub-funds can be automated and controlled. Automation and control eliminates redundant reviews resulting in the greatest impact on accuracy rates.

In a similar way, automating the budget process would allow fund administrators to focus on value add analysis. A fund administrator should be able to do two things while managing the expense processing function: make sure that funds and sub-funds are not materially over-or under-accrued on each valuation date and track an overall expense ratio.

Lastly, U.S. and European fund administrators are in need of a system designed to meet their tax and regulatory reporting tasks. U.S. administrators want consistency between 1099 and 1096 aggregation and a system that can prepare data files for individual funds or at the aggregate trust level. European fund administrators are looking for ease of data files produced for use by internal or external VAT calculation and filing specialists.

So what exactly has been the greatest obstacle in automating expense processing and what are the impacts of that challenge? The greatest obstacle has been the difficulty in moving from expense

processing to a controlled system. Expense processing has little to no industry standardization; many of the tasks have a low frequency, and quite a lot of variability and complexity. As spreadsheets continue to be used, the amount of variability and lack of standards has only made things worse.

When the complex business problem of automating expense processing was lined up with the traditional method of building software, there wasn't much success. The traditional method called for detailed specifications, usually in text, created in advance. A hand off was made to software engineers who then built an application. The end users saw and evaluated the application for the first time months later when it was complete and final, hopeful that the application built matched the end users specifications.

For a simple, standardized task with little to no variability,

maybe this strategy can work. But not for expense processing. A change of strategy is needed. One that uses frequent market interaction, trial and error; build a little bit, then let fund administrators use it, and then build a little more. To make this work, developers will need flexibility in design, scope, and priorities and the ability to change any of them mid-stream.

It is clear that fund administrators are in need of new, cutting edge technology that will reduce errors in their back office operations and improve the quality of the output. In order to be efficient, fund administrators need to have control over their expense processing operations from anywhere and at anytime. The time to automate expense processing is now. MME

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