STP
INVESTMENT SERVICES

BACKSTOP SOLUTIONS®

13 Egregious Mistakes Fund Administrators Make

And the Three Reasons *Why* They Make Them

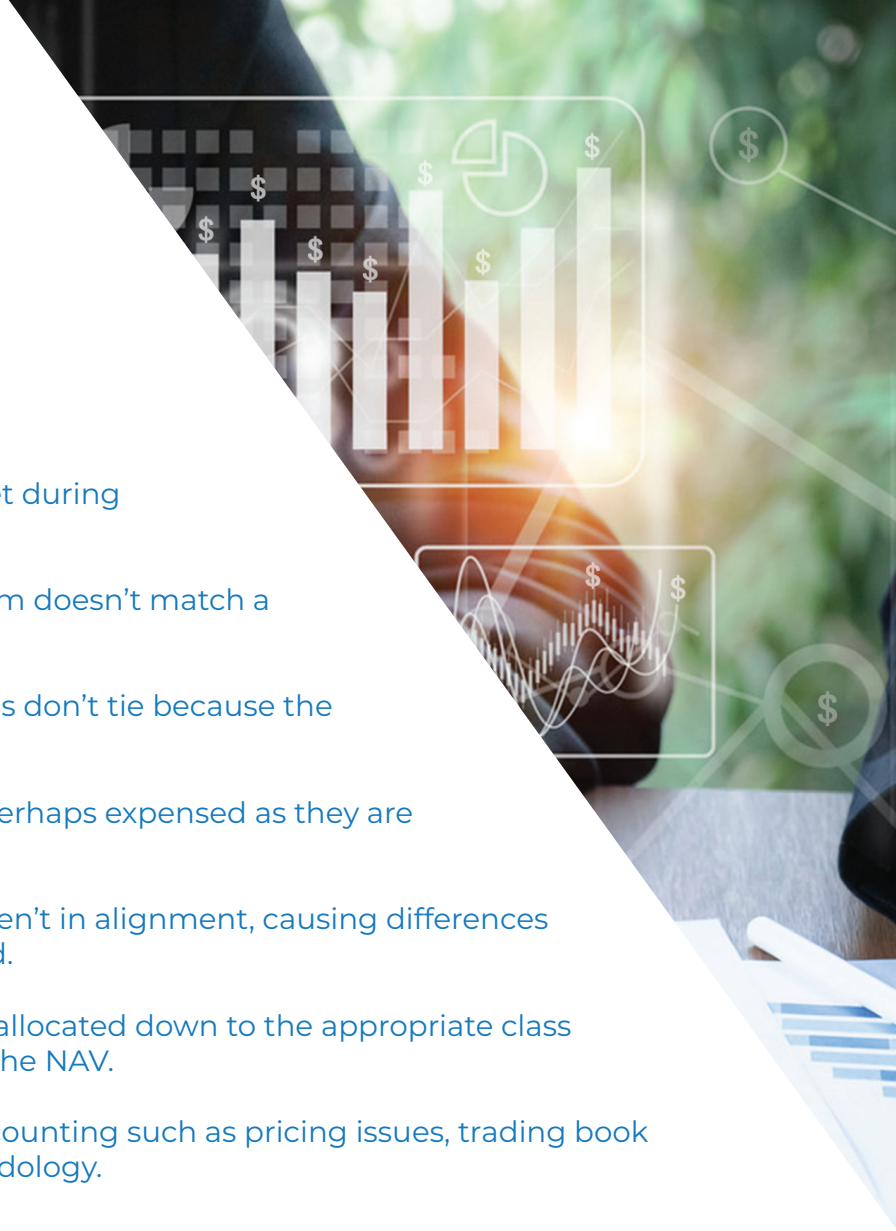
eBook

You only need to look as far as the business headlines to see what happens when fund administrators and management teams make a mistake.

Consider Infinity Q Capital Management. This year, one of its funds, worth $1.8 billion, was shut down as questions emerged about problems with valuations, among other issues. In another case, Calvert Investments paid a $3.9 million fine and $18 million to investors after net asset value, or NAV, errors in 2016.

When you're dealing with millions or billions of dollars, mistakes can add up quickly, especially if fund administrators are leaning on Excel spreadsheets and other manual processes to do the math. At STP, we work with fund administrators to shore up their internal operations, and we see the same errors, miscalculations and omissions pop up all the time.

Here are the 13 egregious mistakes we regularly see fund administrators make:



1. High-water marks are incorrectly reset during crystallization periods.
2. Data in the investor accounting system doesn't match a portfolio's accounting data.
3. Class level and total level trial balances don't tie because the accounting systems aren't in line.
4. Fund expenses are unfairly applied, perhaps expensed as they are incurred instead of accrued annually.
5. Middle office and fund accounting aren't in alignment, causing differences in how accounting entries are booked.
6. Entries in the system aren't correctly allocated down to the appropriate class level, triggering big discrepancies in the NAV.
7. Inadequate controls lead to faulty accounting such as pricing issues, trading book errors and inaccurate lot relief methodology.
8. Incentive fees are regularly applied incorrectly.
9. So are management fees.
10. A bad financial data point on a security master hyper-inflates the principal because the platform's compliance and error checklist was rushed through to get a trade to market quickly.
11. Financial statements don't match investor or portfolio accounting records.
12. Fair and Accurate Credit Transactions Act, or FACTA, filings and Form PF data are incorrect.
13. Corporate action processing and timing leads to discrepancies.

Is your fund administrator making any of these mistakes? More than one? If they are, these errors — costly in both dollars and reputation — often come down to three problems: issues with the systems that track and crunch the numbers; bad or non-existent internal controls to double check information; and a lack of communication between teams as they work with various data sets.

Problem No. 1: Issues with systems

Fund administrators typically have systems set up for accounting or running reports. On their own, those processes may work just fine. But often, they are operating within their own individual silos. They aren't in sync, leading to a misalignment of data sets because all that information doesn't tie.

But alignment problems aren't the only obstacle. Systems can be buggy. And beyond the glitches, some come with other limitations that curb their performance or worse, render them incapable of handling complex and ever-changing data. Kludgy systems can wreak havoc.

Problem No. 2: Lack of proper controls

Many firms don't have the right checks and balances in place to ensure their systems and calculations are accurate.Often, there are no built-in processes designed to make adjustments or improvements as needed.

Instead, individuals are left to do the work, relying on pencil-and-paper calculations or unstructured data in spreadsheets and PDFs that can't easily be queried. As they're analyzing the data, they may not see or understand where there's a discrepancy, either because they're too passive, or because they lack the understanding to know there is a mistake and flag the problem.

But without the proper controls, firms may be missing out on fees, misvaluing assets and making other costly errors. With the right controls in place, they could have easily avoided embarrassing and expensive mistakes. In the case of a bad security master, for example, controls that highlight when a trading price is an aberration of the most recent vendor-supplied market price would avert the error altogether.

Problem No. 3: No communication between teams

Accounting groups, corporate action teams, compliance teams, financial reporting teams — they all have their own data sets. Problems arise when teams don't communicate with each other. One group might pull data without talking to another team, for example, and unknowingly extract the wrong information, or miss out on fully understanding the data they're using to make key decisions.

Regular communication between teams could easily solve these common mistakes. But at large fund administrators where far-flung teams are located across the globe and other processes have been outsourced, teams remain in their own individual silos.

Because the teams aren't talking to each other, nobody can see the big picture behind all the data. Without the proper briefings from those in the know, certain teams might not even be aware of the downstream effects when they rely on particular data points. In other words, risk goes up as communications break down.

Digitized, Scalable, Adopted

Manual processes and human error are often the root causes of the common mistakes that fund administrators make. Even when funds have some form of accounting system, physical processes and Excel spreadsheets may still be used. When a fund doesn't have the right people and systems in place to take care of its books and records, there can be serious consequences.

What funds need, of course, are fewer silos and the elimination of manual checkpoints that introduce unreliable information. The adoption of proactive processes to both check accountability and review controls is vital.

The solution is automation— a partnership between fund administrators and a technology platform that's digitized, scalable and easily adopted. It needs to be user-friendly, even for the least technologically savvy, to reduce manual touchpoints. And it must offer exception-based workflows to strip away the need for as many hands-on processes as possible except under certain conditions.

More than ever before, investors can easily move their money around. No longer are they sticking with the same fund over their lifetime. Instead, they will quickly jump ship at any sign of accounting or valuation concerns. Stability is what investors demand, and funds need to do all they can to demonstrate that they have the right systems, proper controls and appropriate synergies and collaborations in place. When they don't take the time to get it right, they leave a lot on the line — lost money, lost reputation and lost business.

The investment industry makes a lot of decisions based on data. But it's difficult to trust those numbers when fund administrators aren't operating with the right systems, smart controls and proper collaborations among their teams.

At STP, we provide both fund administration and shadow fund administration services to clients to ensure they're not making the egregious mistakes we see all the time. And we do that with the benefit of a Backstop Solutions' product coupled with the STP BluePrint platform that's designed specifically for the fund management industry. Together with our expertise and services and the digital integration benefits of Backstop and STP connectivity, we know our data is reliable, and our advice will only help our clients thrive.

About STP

STP Investment Services is an industry leading global investment operations firm that provides complete front, middle, and back office solutions for investment managers, funds, family offices, wealth managers, and plan sponsors.

To learn more, visit stpis.com.

About Backstop

Backstop Solutions helps the institutional investment industry make the most of every minute. We do this by developing technology to simplify and streamline otherwise time-consuming tasks and processes, enabling our clients to quickly and easily access, share, and manage the knowledge that's critical to their day-to-day success.

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