Why It Pays to Think Through Outsourcing Administration Functions

Fund managers considering shifting accounting and IR processes to a third-party provider should consider the pros and cons before making the move

Greg Myers
Managing Director,
Cortland Capital Market Services LLC

Myers oversees product management for Cortland's fund administration group and has nearly 20 years of broad-based financial services expertise. Prior to joining Cortland, he managed the Specialty Bank Loans team within LaSalle Bank's Global Securities and Trust Services Group.

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Outsourcing functions from a private equity firm to a third party can seem like a great idea: The firm frees up some of its human capital resources for other tasks or can eliminate a position or two and seemingly save money.

But it's important to weigh the pros and cons of making such a move, says Greg Myers, a managing director at Cortland Capital Market Services. He explains that outsourcing internal accounting and investor relations processes can make sense, as a fund administrator can have more robust software and more capacity at peak times to handle accounting functions, allowing the staff at the fund manager to focus on the investment and asset management side of things.

"The inverse is a lot of managers feel they don't have as much control over the day-to-day accounting functions because they've outsourced it," Myers says. "It's more of a perception than a reality. The administrator may have more flexibility on reporting timelines and forms of reports from their systems than the manager may have previously enjoyed or had the capacity to produce. They may not have direct access to information via an internally supported system, but through a cooperatively produced set of periodic reports and the administrators' reporting portal they can get all of their historically produced financial reports and additional management and investor reports not previously available through internal processes."

Aside from the perceived inconvenience of a GP outsourcing some functions, there are other advantages that need to be considered. "You're dependent on a third-party provider," Myers says. "The other risk is that they don't report directly to the manager; it's more of a service-level agreement." However, if you take a step back and look at keeping these functions in-house, there's the risk that as a fund winds down and there's a delay in raising the next fund, "you're going to need to terminate employees and deal with those overhead expenses and HR issues," he says, referring to people who were doing the accounting or other IR tasks.

One of the things that's key for a third-party provider is to have a dialogue with fund managers to see what kind of information they are looking for, Myers says. If they want a lot of reporting, that incorporates more accounting and financial work relating to assets or leverage reporting relating to investors. Reporting stood out to Myers in a trend he's seeing. "The emerging trend, for better or worse, is this idea that crowdfunding or Internet marketing will be a large portion of capital for a lot of funds," he says. "With that, there's the requirement for functionality and transparency that these platforms have that would be difficult for a lot of managers to provide. The difference in reporting information and the corresponding expectations of a $10,000 investor versus a $10M investor is vast, as is the method of delivery and granularity of data."

There's also a continued push to keep investors informed of capital positions, the performance of assets, the expense ratio, and the cash-flow metrics, Myers adds. "It's a fine line between keeping investors up to speed on the performance of their investment without giving them so much detail that the message is confused or lost." ■