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InsideOps | Insights for Asset Management Operations Leaders

Maximizing Due Diligence of Back Office Outsourced Service Providers

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Determining whether to outsource a business function and to whom are important decisions. The results can drive the near and long term strategic path of an asset manager, resulting in significant commitment, risk and investment. Completing a request for proposal (RFP) and review of the service providers' responses is a good way to narrow down the candidates included to a smaller subset, but it is the subsequent due diligence phase that can best be used to prove out the service providers' capabilities and how they fit to the asset manager.

The RFP and its analysis are straightforward processes that have become staples of the service provider selection process, but the due diligence phase can be a little more variable. When such a large investment is at stake, taking full advantage of this phase can make or break the project. Ensuring the firm is organized going into the due diligence phase, has a process in mind, and well-defined objectives are key to exiting with a clear front runner. Incorporating the following elements into the due diligence phase will make this goal a reality.

Formal Agendas and Objectives

The due diligence process is typically a series of in-person meetings between the asset manager's operations team and the service providers' sales and operations leaders.

Recommended practice and experience dictate that the asset manager must play a lead and highly-proactive role in ensuring service providers are well prepared and ready to discuss your priorities at each session. One effective way to accomplish this is to provide formal agendas and case studies to the service providers ahead of time. Depending on the volume and duration of meetings, it may also be beneficial to conduct an orientation session with them to review the agendas, discuss the case studies and set expectations. Although this may sound counter intuitive, it will ensure time is spent on topics and areas that are important to you. The absence of this guidance opens the door for the provider to drive the conversation, which may or may not hit the mark. Providing explicit details and color on the in-scope functions, custom processing requirements, your 24-hour clock, straight through processing rates, proven domain knowledge, or experience with clients of similar size and scope ensures your priorities are covered and ultimately simplifies the decision-making process. An effective way to do this is to provide the service provider with detailed business requirements, process flows and case studies.

For multi-day efforts, providing candid feedback to vendors regarding their presentation performance gives them the opportunity to course correct for future meetings. The bottom line is to obtain the information you need to make a good fact-based decision. Proactively providing clarity regarding business needs, setting expectations and providing timely feedback provides the mechanism to obtain critical information.

It is crucial to take full advantage of the time allotted and, therefore, important to structure the sessions properly. Each meeting or workshop should be dedicated to a specific topic. Depending on the size and scope of the business under consideration, each function may have its own dedicated workshop. In addition, meetings should be scheduled for softer issues such as client service, service level agreements, and on-boarding. The duration of each meeting should align with the topic at hand. Time should set aside for additional follow-ups that may come out of the meetings.

The length of due diligence meetings can span from half a day to multiple weeks.

Business Requirements

For each outsourced function under consideration, having clear business requirements provide an important foundation for assessing each provider's capabilities. Providing accurate, detailed business requirements starts with having accurate documentation of the business function's current state operations. If up-to-date documentation is not available "off the shelf," then a key activity within the service provider selection process is collecting this documentation. The quality of information that can be provided to the service providers directly dictates the quality of information they will provide back. To the extent possible, including information such as cut-off times, formats, communication methodologies, straight through processing and error rate targets are beneficial. This provides the ability to go beyond a perfunctory overview of services and processes and have meaningful conversations about what the provider can and cannot provide.

Use of Case Studies

Case studies are helpful to assess complex business situations using real world examples. Documenting and presenting recent challenges to the service provider gives them the opportunity to demonstrate their knowledge of the matter and present how they handled the situation. In cases that impacted the entire industry - a complex corporate action, for example - the service provider may have had to address this same challenge with their existing clients. Reviewing how they handled this situation and seeing the tools and reporting in action, provides insight into what a "day in the life" with this provider could be like. It also ensures the criteria used to assess the candidates is directly tied to operational issues that could realistically occur. The initial business case to outsource a function could draw directly from realized points of risk that the asset manager has experienced, therefore the selection process should focus on these areas.

Participation by Subject Matter Experts

Another crucial aspect to the meetings is ensuring the right people are at the table; this applies to both parties, service providers and the asset manager. Ensuring the right people are in the room supports discussions and conversations that are meaningful and insightful. Certain subjects require deep day-to-day knowledge of the operations; valuations, corporate actions, etc. are examples of these, while others can be addressed by higher level management such as client service and the proposal review.

Use of Scorecards

Shorter due diligence efforts may not require the formality of a scorecard, but for any meetings beyond a day, a scorecard adds value by standardizing the judging across all participants. Regardless of the scoring methodology used, the scoring should align with the decision making criteria that was established at the outset. Ideally, scoring should be completed immediately after each workshop or meeting. In addition, having an end of day huddle session with the meeting participants to review the scores supports the exchange of observations, insights and the capture of follow up questions. The final consolidated scorecard can be used as an objective measure to support the final recommendation.

Conclusion

Due diligence initiatives are a journey of discovery for both parties involved. For the asset manager, obtaining the most complete understanding possible mitigates risks of discovering gaps during the on-boarding process. For the service provider, it allows the opportunity to validate they can meet the client's requirements and are a good fit for their book of business. When done correctly, both parties go into the deal with eyes wide open, which provides the foundation for a mutually beneficial long term relationship.

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