

MOVING PAST THE INSOURCE VS. OUTSOURCE DECISION

# A NEW MODEL EMERGES

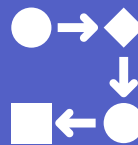


Alternative investment fund CFOs, COOs and IT departments could be excused for looking a little bleary-eyed these days.

As investors continue to increase allocations to the asset class, GPs are finding themselves facing increasing complexity in the back office, as they expand their investor base, number of relationships and investment opportunities. Inevitably, fund managers face questions about how to grow their firms and what systems and processes to keep in-house and what to outsource. Hiring an administrator to manage the back office and reporting functions can help a firm foster internal efficiencies, but not without some much needed considerations around data ownership, security and system integration.

For GPs that are looking to capture the efficiencies of the outsourced model while maintaining control over their underlying information, reverse outsourcing can provide an optimal balance between the insourced and outsourced models. In this administrator-GP working arrangement, the GP ‘hosts’ or owns the accounting and external reporting data and technology, and the administrator utilizes, not their own software, but the GP’s in-house system to assist in the fund accounting and investor reporting function. The admin becomes a true extension of the GP’s back office team. This relationship is facilitated when the GP employs a cloud-based system that allows easy access by all parties, while tightening the GP’s security ecosystem. There are a number of advantages for both parties in this model, most notably as it relates to control, integration, scalability and security.

## Reverse Outsourcing



### CONTROL

Data independence means you stay in control of your information, processes and workflows



### INTEGRATION

Maintaining one single data repository eliminates workflow redundancies



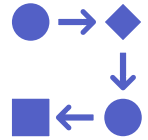
### SCALABILITY

Greater efficiency allows your infrastructure to grow your concert with your firm



### SECURITY

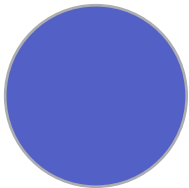
Enterprise-level security and reduced data sharing between fund and admin means less information exposure



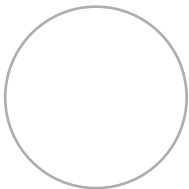
# CONTROL

## Data ownership and supervision stays with GP

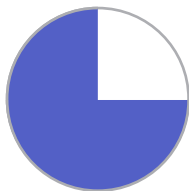
### IMPACT



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When a GP is considering outsourcing their back office operations, it's inevitable that they will lose some degree of control over their processes and data. Established workflows and protocols - valuation procedures, rules, internal checks - will now be overseen by a third party. This can sometimes be disruptive to a GP that has already defined an optimal structure for their back office. For firms still struggling with internal processes, however, an outsourced model can provide a new and improved methodology for those firms seeking best practices. Ultimately, the question becomes whether the GP is willing to relinquish control over how the back office is governed in return for the greater efficiencies and scale an administrator can provide.

Another point to consider is the fact that any underlying data that supports the fund accounting function will now reside outside the firm. This has two ramifications:

- Sensitive information about clients, investments and valuations will now be outside the overview of the GP
- Should the GP want to switch administrators or bring back the function in-house, switching costs will be high as data will have to be pulled and re-formatted to adhere to the new system

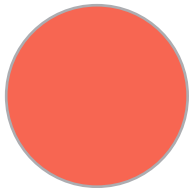
It's clear, for some firms, hiring an administrator can provide a number of benefits. For GPs that want to achieve the efficiencies of the outsourced model but still want to retain their data independence, the reverse outsourcing model can provide the best of both worlds. A GP that opts to retain the fund accounting technology in-house can still maintain full control over their data and workflows while still outsourcing any routine processes through an administrator. This model also provides independence from any one administrator and reduces switching costs should the GP wish to change providers at any point.



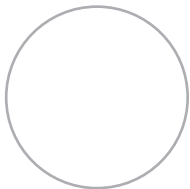
# INTEGRATION

## Flexibility and productivity from a single platform

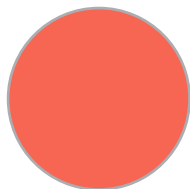
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As a fund manager grows, so does the number of software applications needed to support the firm. Different functions require various types of technologies including:

FUNCTION	APPLICATION
Back office	Fund Accounting
Investment/Deal	Portfolio Monitoring
Client Service/Fundraising	Investor Portals, CRM
Management	Business intelligence

In an insourced or reverse outsourced model where the technology resides with the GP, having all the processes and systems in-house provides the opportunity for system efficiencies vs an outsourced model. Much depends on the type of underlying software being used and the compatibility of the applications to “speak” to one another. Each application, whether it’s a CRM or investor portal, has their own processes but rely on much of the same data. When this data sits in silos in each department’s own systems, you ultimately get redundancy and errors, as data must be pulled and pushed across applications. Often, APIs are developed to bridge the communication gap between systems, but these are often prone to breaking, increasing in operational risk.

When a fund manager moves to a single, integrated platform, a centralized information repository is established, and each application then pulls from a “single source of truth.” Having all information in one place allows your client information and accounting data - across CRM, portal, and investment modules - to share the same data. A hosted, cloud-based system provides the additional benefits of zero maintenance as well as 24/7 and location agnostic accessibility.


When a firm decides to outsource the accounting function, that data is then removed from the GP’s technology ecosystem, preventing the opportunity for system integration and resulting efficiencies. The decision then becomes whether the efficiencies gained from outsourcing the accounting work offsets the challenges of having to maintain two books of records between the GP and administrator.



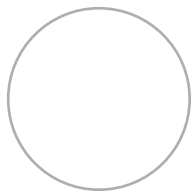
# SCALABILITY

## Increased efficiency allows GPs to scale the business

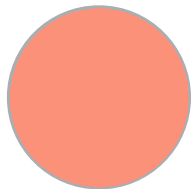
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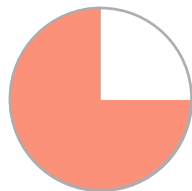
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As a firm grows and expands its client base, strategies and investment opportunities, many firms find it difficult to keep pace with new layers of complexity to the fund structure. New types of investors - pensions, international, ERISA - create additional layers to the operating model from the use of more blockers and entities. Offering co-investment opportunities as well as new funds/strategies further adds to the complexity. A fully outsourced model can provide significant benefits in this scenario as the maintenance of these intricate relationships can be managed by an administrator. It allows personnel to focus on more high-value activities.

In the insourced model, all accounting activity resides within the GP, thus requiring the necessary personnel and technology to support that function. As a firm grows in complexity, however, the bar is raised in hiring qualified personnel to manage the back office activities. An admin can also help address the shifting landscape of both U.S. and European regulations such as GDPR and AIFMD, which can pose a significant burden on a GP.

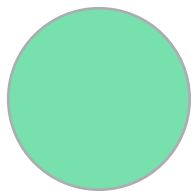
A reversed outsourcing model can often provide the benefits of both the insourced and outsourced models. It allows the GP to offload low-value fund accounting and regulatory work, creating efficiencies in people and processes. The GP still maintains control over their information while expanding the opportunities in acquiring new types of clients. It also increases the capabilities in managing more complex deals and investments. Of course, this increase in scale is predicated on having a technology platform that can optimally manage an intricate web of entity relationships between the GP, LP, investments and operating partners.



# SECURITY

## Reducing information exposure

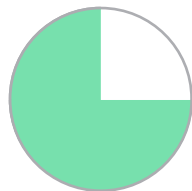
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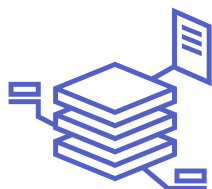
It's no surprise that financial services firms are a prime target for cyber security threats, with the investment management industry no exception. Indeed, the SEC has now made a point of reviewing a fund's security infrastructure as part of their routine audits.

IT security is often evaluated from the perspective of identifying "the weakest link in the chain." There are a numerous vulnerabilities and threats that must be taken into account from brute-force attacks to network penetration.

Information, though, is most vulnerable when it passes from party to party via email, which is inherently an unsecure communication channel - the stated "weakest link." Phishing attacks and the increased use of ransomware to target businesses has its roots in deceiving users through the email. In an outsourced model, information between GP and admin involves the constant sharing of sensitive data between parties, mostly through email. This can expose both firms to the types of email attacks that have gained traction in recent years.

Conversely, maintaining systems in-house, either in the insourced or reverse outsourced model, minimizes the need to share data outside of a GPs domain. In the reverse outsourced model specifically, the administrator logs into the GP's fund accounting platform, greatly reducing the need to email client information back and forth. The use of an investor portal, as part of a GP's technology platform, also reduces the need to email documents to clients and related parties.

## SUMMARY



Traditionally, GPs have had one of two choices when it came to their back office operations: keep it in-house or outsource it to an administrator. Both models have their strengths and weaknesses. The insourced model allows the GP to maintain full control and oversight of their data and information but can lose the efficiencies than an administrator can provide. The outsourced model adds efficiencies and scalabilities, but at the expense of data ownership and control. The reverse outsourced model, with the GP hosting the technology and data internally while utilizing an administrator's manpower, ultimately captures best of both worlds, providing efficiency, scale and control.

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