

Controls Reporting – Helping Irish Asset Managers Compete Internationally

What are the issues?

Irish asset managers who wish to expand their assets under management are targeting international institutional investors such as pension plans, foundations and university endowments. Irish asset managers can expect fierce competition for these assets, not only from rival asset managers but also from hedge funds and private equity funds.

Irish asset managers who are hoping to gather additional institutional assets are looking for ways beyond performance to differentiate themselves from the competition. A recent PwC study suggested that for institutional investors the key driver to invest is not just performance – risk management, compliance and transparency are as important, if not more important than returns.*

The transparent management of risks in a strong control environment is increasingly becoming a key factor in investors' choice of advisor and is therefore crucial for retaining existing customers and a prerequisite to securing new customers' assets, especially US and UK assets.

SAS 70 or AAF 01/06

As customers of asset managers increasingly demand assurance that the organization is operating with adequate safeguards and controls to protect their investments, the internal controls reporting needed to meet this demand can be achieved through:

- the American Institute of Certified Public Accountants' (AICPA) Statement of Auditing Standards No. 70 (SAS 70), or;
- the Institute of Chartered Accountants in England and Wales' standard AAF 01/06.

SAS 70 is the abbreviated term for "Statement on Auditing Standards No. 70: Service Organizations." Issued by the Auditing Standards Board of the American Institute of Certified Public Accountants. SAS 70 outlines the standards external auditors use to assess the internal controls of the service organization and how to report this information to third parties.

SAS 70 has been around for years, particularly for service providers such as fund accountants, custodians and transfer agents. Whilst it is a US standard, it is considered an internationally recognised 'brand'. PricewaterhouseCoopers recommends using this standard if asset managers are targeting US investors or a mix of US and UK investors.

AAF 01/06 is a standard for "Assurance reports on internal controls of service organisations made available to third parties" and is issued by the Institute of Chartered Accountants in England & Wales.

AAF 01/06 is newer standard and is in many ways considered a more flexible framework. PricewaterhouseCoopers recommends using this standard if asset managers are targeting UK investors or wish to include more areas in their controls report.

Either report can serve as a valuable third-party validation that sufficient internal controls are in place and are operating effectively.

In recognition of the significance of controls reporting for asset management organisations, the international asset management industry has been involved in the issuance of specific guidance to provide a standard reporting model for the industry. In the US, Asset Management Group (AMG) of the Securities Industry and Financial Markets Association (SIFMA) have developed recommended baseline areas of scope for controls reporting for asset managers under SAS 70.

Business advantages

The business advantages of such internal controls reporting are twofold:

- What it demonstrates to the marketplace
- Improved operational efficiencies

Internal controls reporting demonstrates that the organisation is proactive in its management of risks and has effective control activities to manage these risks, inspiring confidence and peace of mind in customers and potential customers alike. Focus on the controls over trading and post-trade accounting operations (including valuation) should promote confidence that asset managers are investing according to the investors' mandates or expectations and that investors are provided with accurate and complete reporting of their investments. In addition, the controls report may be helpful in demonstrating good governance not only to prospective clients but also for asset managers seeking outside funding.

* "Transparency versus returns: The institutional investor view of alternative assets" available at www.pwc.com

Investment management and real estate practice

Finger on the pulse

Asset managers will also find that the rigour of the controls reporting process helps them to focus resources on the most important controls while avoiding redundancy and streamlining processes. A strong control environment may also help formalise processes, mitigate risks and vulnerabilities and achieve operational efficiencies and improvements, particularly in areas such as trade processing, valuation and overall risk management. A good control environment ultimately acts as a sound foundation for asset managers to deal with future growth and industry issues.

The steps involved in a SAS 70 or AAF project are:

- Diagnostic evaluation of current controls to identify control gaps or design deficiencies
- Agreement on areas within the control environment that require remediation to address shortfalls
- Remediation of weaknesses identified
- Testing of controls
- Controls reporting and report issuance

It is important to note that the controls reports generally cover procedures common to the operations and accounting for all investors and accordingly, we can typically issue a report which will cover all investors and their investment strategies.

Conclusion

The growing use of the controls reporting process is being driven by the asset management industry and by the market, rather than by regulatory requirements. The implementation of controls reporting is a differentiating factor for Irish asset managers today and should be a strategic priority for firms seeking to compete for international institutional investors.

What sets our SAS 70 service apart?

PwC has an established group of experts, networked globally, with a breadth and depth of experience in the world of asset management. We have significant experience performing SAS 70 examinations for all segments of the industry, including asset managers, hedge fund and mutual fund administrators, transfer agents and custodian banks. PwC uses tried and tested methodologies to deliver a distinctive service.

We are committed to building and developing strong relationships with our clients as a trusted business advisor and our approach is client-centric rather than product driven, focusing on your strengths, weaknesses, opportunities and threats with a view to enhancing and maximising your competitive advantage.

This series presents the PricewaterhouseCoopers point of view on a range of issues affecting our clients and our profession.

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