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# Selecting the Right Outsourcing Partner for Investment Managers

If you were to ask me to choose the next book you should read, my recommendation would have a lot more to do with my preferences than yours. You'll end up knowing much more about me than about the book.

“Disappointment arises from the gap between our expectations and reality. Therefore, it is essential to clearly define our expectations in terms of services, technology, human resources and operational models.”

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If you dislike the book of my choosing, then, at worst, you incur either the inconvenience of returning it or the book's EUR 7.9 price tag. Now, imagine if the cost were 300,000€ per annum, indexed to inflation over the next decade, and an additional 50,000€ to switch to another book. This leads us to the crucial question: Why do we outsource?

As Investment Managers (IMs), our ultimate goal in outsourcing should be to gain peace of mind and focus on our core activities, such as fundraising, marketing and investment management.

When comparing service providers, evaluating fees is relatively straightforward, even though transparency can sometimes be an issue. Assessing quality is far more challenging. The cheapest option is rarely the best, but the most expensive is not necessarily better either. Moreover, when it comes to quality, one size does not fit all. Quality should be defined as the best fit for our specific needs.

## Defining Expectations

Disappointment arises from the gap between our expectations and reality. Therefore, it is essential to clearly define our expectations in terms of services, technology, human resources and operational models. Key considerations include:

- Should we opt for a “one-stop shop” or select the best in class for each function?
- Do we require sophisticated banking services (lending, financing, etc.)?
- What is the typical timeline for investor onboarding?
- What is the average employee retention rate?
- How much is invested in training per employee?
- Are long-term incentive plans offered?
- Which processes are offshored, outsourced or subcontracted and how are they coordinated?
- How is cybersecurity handled?
- How are corporate culture and values defined?
- What are their strategic investments in operational efficiency?

## Potential Pitfalls When Outsourcing

When managers are dissatisfied with their providers, it often stems from issues related to accuracy and timeliness. Receiving reports late is frustrating; receiving them late and incorrect is unacceptable.

Some managers struggle to reach the person in charge, so their grievances about insufficient responsiveness or a lack of complaint resolution ultimately fall on deaf ears.

Minor negligence can lead to costly consequences, such as:

- Missing the cut-off time for a payment related to a deal
- Forgetting to send an invitation to a board member for an investment committee
- Sending an urgent request to a US-based deal team on July 4th

Such events can tarnish the management company's reputation and impact LPs.

According to Preqin, 23% of IMs changed their Fund Administrator (FA) in 2019 due to the following reasons:

- 56% were dissatisfied with the quality of service
- 33% were concerned about cost
- 11% were influenced by investors' concerns about the service provider

## The Cost of Getting It Wrong

"If you don't have time to do it right, when will you have time to do it over?"


Selecting the right business partners is time-consuming and costly. The due diligence process involves several steps, including:

1. Establishing the Due Diligence Questionnaire (DDQ)
2. Compiling a long list of potential providers
3. Performing a Request for Information (RFI)
4. Shortlisting the contenders
5. Performing and analyzing the Request for Proposal (RFP)
6. Comparing fee proposals
7. Negotiating fees

Failing to choose the right business partner will cost you much more and generate frustration. IMs will bear the cost of migration and pay both providers during the parallel run. And, as mentioned earlier, the hefty price tag of choosing the wrong provider can also include additional lost funds and reputational damage.

## Fair Price, Total Cost, and Value for Money

While everyone wants the best price, it is also crucial to ensure that the price paid is fair and sufficient for the service provider to deliver sustainable quality. Additionally, it is key to look at the total cost. Consider two proposals for a EUR 300 million fund.

The first one (P1) costs EUR 300,000, and the second one (P2) costs EUR 330,000. P2 charges 10% more than P1, resulting in an additional cost of EUR 300,000 over 10 years. This is just 1 basis point (0.01%) on a EUR 300 million fund. For a fund's gross performance of 10%, the net performance will be 9.89% instead of 9.90%. 

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The success of your private equity fund and your investments is highly dependent on compliance with increasingly stringent and ever-changing legal and tax regulations.

Whether you are a private equity or venture capital fund manager, a professional investor or a high-net-worth entrepreneur, you can rely on us to understand your needs and provide you with innovative solutions to reach your ambitions.



# Understanding your PE-rspective, our FUND-amental principle

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➔ In addition to the fees paid to the service provider, some IMs need to hire accountants to verify, validate, and correct reports from their FA.

#### Different Shades of Outsourcing

Unlike the European market, the American market remains predominantly “insourced.” These IMs administer their funds on their own platforms. Some find the outsourcing model too radical and opt for the “co-sourcing” model. In this model, one or several FAs work remotely on the IM’s systems. This approach enables IMs to maintain full control over their data and monitor their global risk exposure, regardless of who is administering them. It also provides more control over quality and reduces switching and migration costs.

This model requires FAs to train their teams on multiple IT platforms. Significantly reduced migration costs incentivizes service providers to deliver excellence. Some American IMs push this model when working with European service providers too. Yet, it is not easily transposable in Europe due to regulatory constraints, such as data protection.

#### Conclusion

Selecting the best, or at least the most fitting FA takes time and incurs costs. Choosing a suboptimal service provider will cost much more. Poor quality can impact the fund, its LPs, and

result in audit overruns. Migrating to a new FA also demands time, energy, and money. Therefore, selecting the right service provider should be seen as an investment, with peace of mind as the reward.

Additionally, appointing a local independent Non-Executive Director (NED) to monitor the service provider may also be beneficial. In the end, the goal is to ensure that the service provider meets our needs and maintains high standards, ultimately contributing to the success and reputation of the investment management company. ●

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