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Unlocking the Power of the Turnkey Mutual Fund Platform

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Although investment vehicles continue to evolve and expand, mutual funds remain one of the most popular vehicles of choice by U.S. investors, with \$11.621 trillion in assets. Because mutual funds are so widely available and embraced by a variety of investors, asset managers and fund advisors are constantly looking for an optimal method of launching new mutual funds, so that their investment strategies can reach a greater number of investors.

The increasing demand for specialized or niche investment strategies has continued to spur new developments in the mutual fund marketplace, as asset managers respond to investor interest in emerging markets, commodities and hedge-like products.

At the same time, however, the financial services industry is facing a challenging market environment and increasing regulatory oversight. The past decade has seen several significant changes in financial regulations. For example, the **Sarbanes-Oxley Act** was introduced in 2002, requiring tighter internal controls within publicly traded companies and investment companies and mandating that company officers evaluate and certify to their internal controls. In 2004, the **Securities and Exchange Commission** issued **Rule 38a-1**, requiring the adoption of policies and procedures to help prevent violations of securities law and the designation of a chief compliance officer (CCO) for fund complexes. New requirements can often necessitate additional resources, taking the focus away from the core asset management business. These challenges may be one reason why the

number of mutual funds available in the U.S. has ultimately declined over the last 10 years. According to the **Investment Company Institute**, there were a total of 7,581 mutual funds in 2010, compared to 8,155 mutual funds in 2000. Faced with growing price competition and investors' demands for lower fees, asset managers are looking for ways to reduce their costs of doing business in order to maintain their profit margins within a highly competitive market.

Preparing for a New Fund Launch

There are several decisions an asset manager must consider before deciding to launch a new mutual fund. The manager must appoint a board of directors and officers for the fund. Service providers will be required for fund accounting and administration, custody and transfer agency. Fund counsel and a CCO must be hired, as well. The success of a mutual fund launch often depends on getting to market as quickly as possible. Establishing these functions in a timely and cost effective manner is the primary goal and objective of any mutual fund launch.

In addition to the asset manager requiring added resources, the changing regulatory environment can be a significant hurdle to a successful fund launch. While most fund advisors are familiar with the **Investment Advisers Act of 1940**, they may be less familiar with the requirements of the **Investment Company Act of 1940**, which governs mutual funds. It can be a large hurdle for a fund advisor to become familiar with these laws so that the new fund is compliant.

In addition, investments into technology and systems that provide oversight with respect to these regulations can become quite costly.

It is easy to see why, in many cases, a small- or mid-sized asset manager would find it difficult to set up a new mutual fund independently. Operating within an environment of time and resource constraints can create additional pressure on the manager, taking time away from the most important aspects of his or her money management business. For these reasons, it may make sense to use a turnkey solution.

The Turnkey Solution

Turnkey mutual fund platforms have many advantages, allowing an asset manager to leverage and benefit from a mature, existing fund offering with established resources. The turnkey has in place an existing board of directors and fund officers, board governance procedures, a CCO, outside counsel and a fund auditor. By offering access to a comprehensive suite of services, the turnkey helps manage the day-to-day operations of a mutual fund, such as fund accounting and administration, transfer agency and custody. Asset managers also benefit from the turnkey's existing selling agreements with broker-dealers that distribute the fund.

Compared to a standalone fund launch, the turnkey platform's bundle of services helps save time, reduce expenses and increase scalability. For example, mutual fund launches with a turnkey solution take approximately 120 days on average, while standalone launches may take up to six months. On



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the cost side, the average cost for hiring outside counsel to launch a mutual fund on a standalone basis can be as high as \$150,000, because there is more organizational work to be completed for this type of launch. In contrast, the cost of outside counsel to help launch a mutual fund on a turnkey platform is generally less than \$40,000. Since the turnkey functions are already established, there is no need to create a new trust or organizational structure before launching a fund. Instead, utilizing a turnkey solution allows asset managers to leverage high-quality service and expertise while focusing on managing investments for their funds.

The use of a turnkey fund structure is gaining momentum not only for new mutual funds but for existing mutual funds, as well. Existing mutual fund sponsors have been faced with market volatility, depressed investment returns and declining asset values. In addition, money market fund sponsors have been negatively impacted by reduced interest rates. All of these factors translate into lower investment advisory fees and increased fund subsidies, leaving fund sponsors to look for strategic alternatives to managing the cost structure for their fund complexes. As a result, existing mutual funds are becoming increasingly interested in gaining access to the benefits that a turnkey platform can offer.

What to Look For In a Service Provider

While many service providers offer similar capabilities, there are certain differentiators that can set a turnkey solution apart from its competitors. It is important that a service provider be well-established in the turnkey business, with a dedicated team of professionals and a comprehensive process for executing fund operations. The offering should deliver a complete solution to asset managers, regardless of their size, and it should include all of the neces-

sary core services such as fund accounting and administration, transfer agency and custody. These services can be even more valuable if they are combined with other functions that the service provider offers, such as performance and risk analytics, middle-office outsourcing and transition management. Finally, the

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service provider should display its leadership through participation in industry committees, advocating for clients on discussions around regulatory change and industry oversight.

"We have found that experience is of the utmost importance when selecting a service provider," said **Brett Sumsion**, Chief Commercial Officer and Managing Director, Asset Allocation of **DuPont Capital Management**. "Our provider, **BNY Mellon**, has a highly experienced team in place that advocates for our success. Their turnkey solution provides key services that help us expedite our fund launches and manage day-to-day fund operations, allowing us to focus on managing money."

Technology can also be a significant differentiator when choosing a service provider. For example, a service provider that relies solely on its own technology and professionals to handle the core services of its turnkey solution can improve communications and create efficiencies, such as straight-through processing. Many service providers are also examining ways in which new forms of technology can be used to obtain faster, more efficient processing. Utilizing best-in-class surround technology allows

service providers to further improve their processing capabilities. "A fund advisor can buy software for in-house use to help with these regulatory requirements, but it will also need to invest in a skilled employee who is comfortable with using the software," said **Salvatore Faia**, President of **Vigilant Compliance Services**. "An effective service provider will already have up-to-date technology and a skilled team that the adviser can use to maintain compliance with securities and tax laws."

Summary

The current economic and regulatory environment has proven to be challenging for asset managers. Post **Sarbanes-Oxley**, the industry has seen an increased demand by asset managers for solutions to help them alleviate the rising costs and increasing time to market that these new regulations bring. Many asset managers are discovering that using a turnkey platform to launch and maintain funds can be a time-saving and cost-effective solution. By leveraging the turnkey solution's existing fund structure and established and proven resources, asset managers are better able to manage the regulatory, compliance and day-to-day operational challenges of a mutual fund. Partnering with the right service provider can create efficiencies, lower costs and allow more time for managing investments and focusing on client relationships.

As Managing Director and Head of U.S. Fund Accounting and Administration for BNY Mellon Asset Servicing's U.S. Funds Services group, Jay Nusblatt oversees fund accounting, tax and regulatory services for mutual funds and other investment company clients. Mr. Nusblatt received a Bachelor of Science degree in accounting from Babson College and a master of business administration degree in finance from Philadelphia University. He is also an active participant and a frequent speaker at industry conferences.