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UPCOMING EVENTS

- December 10: Asset Manager, Custodian, and Vendor conference calls (details sent via e-mail)
- February 12: AMF Accounting Workshop
- February 13: AMF Quarterly Meeting
- March 16: Mutual Fund Workshop
- May 21: AMF Operational Risk Management Workshop
- May 21: AMF Quarterly Meeting

Industry Professionals Share Ideas and Strategies at the AMF Quarterly Meeting

The AMF hosted its third Quarterly Meeting of 2003 on Tuesday, October 21st. Over 50 members from nearly 30 firms were in attendance. The all-day event featured committee updates, panel discussions, and vendor solution presentations and included the annual compensation survey. Below are highlights of the event.

AMF Benchmarking Committee

Paul Fehre of New York Life, Chairman of the Benchmarking Committee, presented preliminary results from the committee's MBS Processing survey to the Forum. The Survey was distributed to member firms on October 2nd and was requested to be returned by October 31st. Results were presented from 11 surveys that were received (approximately 30% of distributed surveys) and contained data that reflected the following:

- Processing statistics for MBS – including reconciliation frequency, settlement rates, and volume of MBS processed annually
- Custodian and broker data – including number of custodians firms deal with for MBS, percentage of accounts on a contractual settlement basis, and method of notification of fails by custodians and brokers
- Systems use – including use of EPN, various systems used to process MBS by function, and vendors utilized for MBS DATA
- Staff statistics – including number of FTE's required for MBS processing by function and average experience

Once all surveys have been received, members of the Benchmarking committee will analyze the data and release the results to the general membership. Any member firm who has not received a survey should contact Diane Trupia at dtrupia@bondmarkets.com.

AMF Straight-Through-Processing Committee

An update on the STP Committee was presented by Committee Chairperson Christine Sumner of Pacific Life. Christine discussed the committee's work with the BMA's Common Message Hub initiative, combining the services of the SIAC SFTI network and the DTCC's SMART network.

Committee member Larry Barnett presented his work on interpreting the recent FICC white paper on mortgage netting for buy-side firms. Larry has interviewed member firms and met with the FICC with the goal of figuring how to make mortgage netting work for buy-side firms.

The committee will discuss next steps for each of these initiatives at their next meeting scheduled for sometime this month. For more information or to participate in this committee, please contact Diane Trupia at dtrupia@bondmarkets.com.

Fails Management Panel Discussion

The central themes of the panel discussions were clearly standardization and communication – and the standardization of communication.

Moderator Chris Coleman of Investors Bankers & Trust led panelists Lance DeLuca of BlackRock, Frank Malarkey of CSFB and Kevin Morrissey of State Street in a discussion that addressed the issues in the industry that are causing fails and suggested ways to improve the current process so that the fail rate can be reduced.



Chris Coleman, Lance DeLuca, Frank Malarkey, and Kevin Morrissey discuss Fails Management

There were many issues that caused fails discussed during the 90-minute presentation, including verbal confirmation, incorrect delivery instructions, missing date on trade instructions to custodians, and untimely post-settlement reconciliations. These issues spanned all branches of the industry, though affecting each in different, though relational, ways. The lack of standardization in the communication of confirmations, delivery instructions, and fail reports were at the root of the industry fail rate. The membership discussed the importance of various automated vendor solutions and best-practices, but agreed that it would be necessary to have buy-side, sell-side, and custodians at the same table if the issues were to be solved.

The AMF, through its STP Committee, will continue to work on researching solutions to these issues, capitalizing of the diverse representation of its members to better formulate industry-wide solutions.

Claims Panel Discussion

The panel discussion on claims was led by Jason Cronin of Wellington Asset Management and included William Filunok from Bank of New York,

James Glover of RBS Greenwich Capital, and Joe Pomo of GSAM.



Jason Cronin, William Filunok, James Glover and Joe Pomo on the Claims Panel

Concerns addressed during the discussion circled around the standardization of best practices. The Forum and panel addressed the use of ISITC's Claims and Compensation best-practices document (available on the ISITC website at www.isitc.org). But it was noted that many firms do not use and/or do not follow the practices listed in the document – especially in the domestic market.

Some firms felt that one of the issues of most concern was the rate of interest being charged. While the standard domestically is usually the fed funds rate (now at 1%), some felt that the amount was not enough to cover the cost of processing the failed trade and the resulting claim. And because the cost of claims has been mitigated due to the low interest rate, firms are less concerned about fails that may result in claims, possibly resulting in a higher rate of fails over more than one day.

The discussion came to a similar conclusion as the Fails Management panel, stressing the importance of using the STP Committee has a means to bring the industry together to address pertinent issues.

Corporate Actions Panel Presentation

Jason Jesner of CSAM led a panel of presentations on Corporate Actions, beginning with a model that the AMF Corporate Actions Committee developed two years ago. While the complexity of the corporate action process continues to be a concern of asset management

firms, there has not been much development in the process since that time. Asset managers are continuing to experience difficulty handling the processing of corporate actions, a manual process often requiring several staff. The issues again circle around the standardization of the information provided on the corporate actions and the communication process that is involved. While the SIA is working with the SEC to create regulatory standards, firms that have to deal with corporate actions on a daily basis are finding it difficult to devote the necessary time and resources.



Jason Jesner, Lorraine Morrison, Craig Schachter, and Vincent Greco discuss Corporate Actions

Lorraine Morrison of the DTCC and Craig Schachter of Xcitek presented vendor solutions for the processing of corporate actions and the compilation of corporate action information into a central database. The DTCC has published a paper entitled "Transforming Corporate Actions," which is available at <http://www.dtcc.com/ThoughtLeadership/whitepapers/GCA%20White%20Paper.pdf> The paper focuses on several issues including:

- Processing challenges
- Managing risk and cost
- Obtaining accurate information
- Managing flow of information
- Second-sourcing
- Handling complex instruments
- Using information from multiple sources
- Staffing skill and expertise
- Processing the elections

The DTCC is also working on a central Corporate Action repository – a library which would be available online. The repository would act as a data scrubbing and validation source. Xcitek

provides a Corporate Action information service – validating data and providing that data to 300 firms.

Steering Committee and Annual Compensation Survey

The AMF conducted its second annual compensation survey designed to identify high level trends in employee and management compensation. This year survey showed a higher salary and bonus increase (as a percentage) than last year, while overall staffing levels remain steady or slightly decreasing. Anyone interested in receiving a copy can send a note to Diane Trupia at dtrupia@bondmarkets.com.

Nominations for the Steering Committee are being accepted to fill three open seats. Voting and a final decision will take place on or about November 30th.

AMF Hosts Project Management Workshop

The AMF hosted a Project Management Workshop on October 20th. This first "non operational" workshop was well received by the attendees. The day featured two panels discussing The Components of Project Management, moderated by Larry Barnett. Panel members included Connie Chen, DTCC, Paul Fehre, NY Life Investment Management and Chris Milner, Appix. The second panel discussed "Ensuring Project Management Success." This panel was moderated by Jerry Hill, ESI International. Panel members included Tom Fortin, BlackRock, Paul Parseghian, Prudential Investment Management, Michael Rucci, Goldman Sachs Asset Management and Adam Schneider, Deloitte & Touche.



Program chair Lisa Ilaria introduces panel members Larry Barnett, Connie Chen, Paul Fehre and Chris Milner

Steve Gould, a Project Management professional was the Keynote speaker. Steve spoke of the various leadership qualities and provided insight on how to successfully lead a project. The day closed with a case study where the attendees participated in a simulation of a conflict between co-workers that resulted from poor management within the organization.

The AMF would like to extend its Thanks to the moderators, panelists, our Keynote speaker and Diane Trupia for all of her efforts in ensuring that the day ran flawlessly!

Improving Middle Office Efficiency

The middle office plays a critical liaison role between the investment manager, traders and their brokers, as well as external counterparties such as custodians, non-U.S. depositories, Depository Trust & Clearing Corporation (DTCC) and clients. The objective is to ensure accurate and timely trade processing and communications to any party who needs to receive the trades.

Many asset managers still operate middle office functions that are paper based and labor intensive. For example, coordinating trade confirmations with multiple custodians still happens via phone, fax or workstations. Such processes require a good deal of manual intervention, which can lead to errors and increased costs. In addition, some investment managers face the burden of supporting multiple legacy systems running from different databases.

Streamlining data flow

The key to maintaining a smooth operation is efficiently managing the data flow among various systems, including portfolio management, trade order management, custody/fund accounting and corporate actions, to name a few. To accomplish this, a middle office must streamline the following:

- Automated trade confirmation/matching
- Automated and standardized trade interfaces to custodians, clients and other third parties
- Automated processing of trade cancellations and corrections
- Compliance of trade activity with clients' objectives
- Exception based reconciliation of cash and holdings
- Corporate actions processing

- Consolidated management reporting of all trade activity
- Cash management

Middle offices must also standardize and consolidate the varying protocols and reporting capabilities of all parties in a given transaction. For many operations, this means further enhancements to message routing technology, middleware applications and standardized electronic interfaces.

Improving middle office operations yields tangible benefits. For example, upgrading to a superior reconciliation system means any discrepancies can be identified and resolved sooner, which cuts down on failed trades and market exposure, and allows more time to focus on exception management and risk reporting. An advanced corporate actions system will expedite notifications, integrate all processing onto a single platform and help ensure that no corporate action opportunities are missed.

Each investment manager must assess the value of maintaining these demanding operations internally versus outsourcing to a service provider who has committed to continual investment in automated processes and the latest technology. For more questions about improving middle office efficiency, please contact Paul McGuiggan, Senior Director, Investors Bank & Trust, at 617 937-6246 or PMMcGuiggan@ibtco.com.

The above was contributed by Don Eng of IBT.

AMF Accounting Policies Committee Addresses Inconsistencies in Implementation of FAS 149

The AMF Accounting Policies Committee held a conference call on November 5th to discuss the implementation of FAS 149, a recent accounting regulation surrounding mortgage TBAs. Elias Habayeb of Deloitte & Touche offered an overview of the position taken by the Big 4 accounting firms on the application of the regulation for insurance companies and led a discussion of the topic. On the call were insurance company member firms and asset management member firms who manage money for insurance companies.

The original FAS 133 regulation outlined accounting rules indicating when TBAs had to be treated as derivatives. FAS 149 was intended to clarify the general statements made by FAS 133 by outlining the criteria that needed to occur in order to determine if a TBA should be treated as a derivative. If a firm is required to report on a trade-date basis (as dealer firms are) the TBA would not be treated as a derivative. The complexity starts when this is not the case, as is the issue with Insurance companies. If a firm does not have to report on a trade-date basis there are 3 additional criteria that must be met in order for a TBA *not* to be treated as a derivative:

1. This is the only way to obtain the security;
2. The TBA will settle in the shortest period possible; and
3. It is probable that a firm will take delivery of the pools.

The problem for insurance companies and asset managers who manage money for insurance companies has become that there is no consensus among the major accounting firms in how to apply these accounting rules.

On the call, the members of the Accounting Policies committee and Mr. Habayeb discussed how to address the issue of this inconsistency. Several ideas were raised, including the possibility of addressing the issue to the AICPA or the FASB. The conference call adjourned with the decision made to follow up on the issue and decide how and who to approach on assisting with the issue.

For more information on the Accounting Policies Committee or to participate, please contact Diane Trupia at dtrupia@bondmarkets.com.

FASB Releases Modification of Interpretation 46

On October 31st, FASB issued a modification to the original accounting interpretation (No. 46) it had made regarding Variable Interest Entities (VIEs). The FASB issued the modification after industry response to the original interpretation indicated that firms were having difficulty implementing the new accounting regulations.

Interpretation 46 has been of particular concern to the members of the AMF because of the affect on asset management firms who issue CDOs. The new regulations would require that any enterprise that can be determined to be the

primary beneficiary of a VIE (of which CDOs are one) must consolidate the assets and liabilities of the CDO on their balance sheets. Though FASB outlined the criteria to be used in the determination of a primary beneficiary, interpretation of the rule by accounting firms has been inconsistent and confusing to their asset manager clients. The AMF has held numerous conference calls to discuss the application of the regulations after the release of the interpretation, and was active in lobbying for changes to the draft of the original interpretation last year.

The FASB is asking the industry to submit comments on the modifications by December 1st. The AMF has not yet decided whether or not to further comment on these modifications.

Buy-Side and Sell-Side Come Together over MBS Concerns

One positive outcome from the recent MBS fails situation has been the community that is being built between buy and sell-side firms. At the recent BMA-sponsored Fixed Income Operations Conference and MBS Operations Seminar, members of the AMF noticed that it was important to the sell-side that they work with buy-side firms to resolve issues surrounding this complicated topic. One member noted, "This sense of community and the cooperation that it has fostered has made it possible for everyone to better partner during a time of change and challenges within the MBS market."

The number of MBS fails that have occurred in recent months has affected the entire industry and has resulted in many round-robin conference calls. This was an important issue of discussion at both the conference and the seminar series. Solutions were discussed that are intended to reduce the frequency of fails, and reduce costs and risks, things that would benefit firms on both sides of the fixed income market. Among these were trade and pool netting, Straight-Through-Processing, and the standardization of the MBS trade "lifecycle". The AMF STP Committee has already began to take steps to understand these solutions by talking with the FICC and working to interpret the recent *STP for Institutional Settlement* white paper.

One of the goals of both the BMA and the AMF has always been to facilitate the relationship between buy-side and sell-side firms. Issues like

STP and MBS processing are the examples of how this common goal is succeeding.

Perspectives: Meeting the Requirements of Portfolio Reporting and Reconciliation Initiatives

The following was written in response to the Perspectives article last month. That piece addressed the importance of accurate daily custodian reporting to asset manager cash management. This response is taken from the Custodian Perspective.

As part of their overall STP initiatives, Global Custodians continue to enhance their existing reporting platforms to support a varied set of requirements from investment management firms. These initiatives have included further build-out of web-based reporting products that provide easy accessibility and system integration to customized report data. Furthermore, additional work is being done via the ISITC-IOA reconciliation sub-committee to develop and refine industry standards for statement reporting via SWIFT. For example, updated versions of the ISITC 950 and 535 statement message types have been recently agreed upon by ISITC-IOA members.

The frequency in which an investment manager reconciles cash and assets can vary depending on the investment strategy of the portfolio and the frequency in which the security positions are turned over. If the reporting requirements for an investment manager are communicated effectively, a reporting package can be constructed to support either a daily, weekly, or monthly reconciliation of cash and/or assets. Many buy-side firms today are using a combination of SWIFT statement advising, and a supplemental report package made available via a global custodian's proprietary information delivery platform. For firms who do not have access to the SWIFT network, other communication interfaces can be supported, either through a file transfer protocol from a custodian's proprietary reporting platform or via another vendor service such as the DTC-Hub.

The majority of the global custodians also maintain relationship and service teams around their investment manager clients (i.e., mutual funds and separate account institutional asset portfolios). This enables them to work closely

with their buy-side relationships to define reporting requirements, as well as develop cash management procedures to support a daily reconciliation of cash. For example, a portfolio trading in money market instruments settling same day requires a different level of partnership between the investment manager and global custodian. This will ensure that all trades have been communicated and processed timely to enable an accurate daily investment of available cash. Desk procedures can also be refined based on specific relationships to support a due diligence process around overdrafts and positive balances based on client/account profiles.

Generally speaking, friction points that may develop in a daily cash reconciliation process between an investment manager and global custodian can be minimized or eliminated when both parties work together to ensure that reporting requirements are well defined, and feedback is maintained on a continuous basis. When that type of partnership is developed it becomes much easier for all parties to succeed in an information delivery business.

The above was contributed by a custodian member of the AMF and represents a collaborative custodial viewpoint.

Ask the AMF

Why Should I Do Benchmarking Surveys?

AMF members seem torn on the subject of benchmarking surveys. They all want to know what other firms are doing about compensation and what their fails rate might be, but no one wants to spend the 10 minutes to answer a survey. Why should you answer a survey instead of waiting for everyone else to do it? Because you can then compare your answers to the results and get free consulting services! You also can use it as a reality check against your metrics (or as a basis for metrics if you don't have any). Most of the surveys take less than 10 minutes to complete, and many of them can be done without assembling a whole team of colleagues. Best of all, senior management loves benchmarking results, so you can use it to help justify your AMF membership (though that shouldn't be a problem if you're on a committee and go to the quarterly meetings and seminars), and you can use it when you need more

automation in mortgage processing or STP infrastructure. If you need survey results to press a specific concept with management, contact us and suggest a new benchmarking topic. Speaking of surveys, if you're a member and haven't completed the member survey, go to www.theassetmanager.com/survey.html and spend 5 minutes filling in a basic survey on why people are members of the AMF and what they want to get out of it.