

## In Transition

### *Managing the Costs of Going Global*

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In the more than two and a half years since the removal of the Foreign Property Rule, Canadian plan sponsors have been reducing their domestic exposure in favour of international mandates. For some, this has meant entering new markets and managing substantially more complex transitions than they had in the past. International asset movements typically involve multiple jurisdictions, counterparties, currencies, time zones, and settlement conventions. Unmanaged, the risks associated with this increased complexity can erode the value of plan assets. Plan sponsors may be faced with explicit costs that are as much as 30% higher than they've been accustomed to in North American transitions.

### **Don't assume**

Global transitions require exceptional care and simply asking managers of new investment mandates to handle the transition can produce inconsistent results. Doing this assumes that the managers have low-cost commission structures, familiarity with legacy securities, and an expertise in short-term risk management techniques. Trade optimization programs, order management systems, and access to multiple sources of liquidity are not the traditional focus of investment managers. However, these factors are integral to the transition management process. In addition to the quantitative tools required to manage the risks and reduce the costs of global transitions, project management skills are needed to manage the operational risks involved. They allow the transition manager to coordinate the activities of the numerous stakeholders including plan sponsors, consultants, investment managers, and custodians, and to maintain contact with the various regulatory bodies in the countries where assets are to be traded.

### **Expect the unexpected**

Some of the operational challenges facing plan sponsors when moving assets internationally can come from unexpected sources. For example, although sub-custodian accounts can be opened in most countries in a matter of days, in some circumstances, if there is no pre-existing account to which to link the new one, trading can be delayed for weeks. Opening a sub-custodian account in Venezuela, for example, can take as much as six to eight weeks. Even more daunting is the prospect of opening an account for the first time in India or Taiwan, where a plan sponsor may be required to hire a local tax consultant to complete the process.

The taxes and fees imposed by some countries on the transfer of securities can also contribute to increased transaction costs. Even events that are normally free of explicit and implicit costs, such as in-kind transfers, can attract taxes. In the case of pooled funds these transactions may even be subject to double taxation. Special care must be taken to avoid any unnecessary change in beneficial ownership.

Maintaining the appropriate benchmark exposure, a tenet of the transition management process, can be a greater challenge in global transitions. While securities generally settle on a trade date plus 3-day cycle, this is not true in all countries. For example, South Africa settles on T+5 while Germany and Hong Kong both settle on T+2. In Taiwan and South Korea, purchases cannot be initiated until the exchange verifies that an investor has posted sufficient funding in the local currency. The cost of buy-ins and settlement penalties in some countries can be high, and experienced transition managers pay particular attention to local holidays and varied settlement cycles to avoid fails.

Finally, additional consideration must be given to securities that are difficult to transfer, securities on loan globally, and derivative positions in legacy portfolios. Improperly managed, each can extend the transition's trading horizon and increase opportunity risk. Unless the transition manager is able to handle these operational issues as well as the portfolio management and trading responsibilities, the plan may face unnecessary risk and expense.