What is ASP?

KELVIN WALTON ASKS THE DECEPTIVELY SIMPLE QUESTION: WHAT IS AN APPLICATION SERVICE PROVIDER?

Executive summary

- **This article – the first of two – reviews the fundamental principles of treasury application service provision, and analyses the model's applications and value, primarily from the perspective of an entry-level treasury operation.**

Application service provider or ASP is one of those technological terms that do not immediately convey deep meaning to non-specialists. In fact, there is no simple or fully accepted definition of ASP, but in the context of corporate treasury operations, an ASP solution will have all or most of the following characteristics:

- The treasury management system (TMS) is hosted by an external company, which may be a sister company of the ASP or a third party;
- The ASP takes care of database setup and administration;
- The ASP provides technical support;
- The users access the TMS via the web;
- The client pays for the service via a subscription, which covers the software licence, hosting, and application and technical support;
- The contractual agreement is flexible over a fixed term; and
- The client's treasury technology needs are basically standard.

This list contains far more technology and contract jargon than treasury-related terms, suggesting that the decision to select an ASP solution is primarily driven by technology considerations. This hypothesis will be examined later in this article, but first let's look at the treasury-related elements of ASP evaluation.

WHO NEEDS A TMS? Little more than 10 years ago, few UK companies outside the FTSE 150 would invest in TMS technology. Today, the market has deepened substantially, for a variety of reasons, including better understanding of the value of expert cash and risk management, tightening audit standards (and the consequent demands by management for robust, complete and timely financial reporting). Today, companies with turnovers of £250m and upwards are likely to operate treasury departments; and all treasury departments are vulnerable to auditing and management pressures to implement professional treasury technology to support their operations.

Treasurers may be evaluating the ASP option as a secure, swift and cost-effective means of acquiring an entry-level TMS. But do a given treasury department's system requirements really fit the ASP model?

"I RUN A BOG-STANDARD TREASURY" This observation sends shivers through experienced treasury consultants, because in practice no two treasuries are identical. Even within the same industry sector, departments may be utterly different because of radical differences in gearing, say. ASP solutions are structured to be rolled out with little or no client-specific customisation, but every treasury will have some specific requirements, primarily in the following areas:

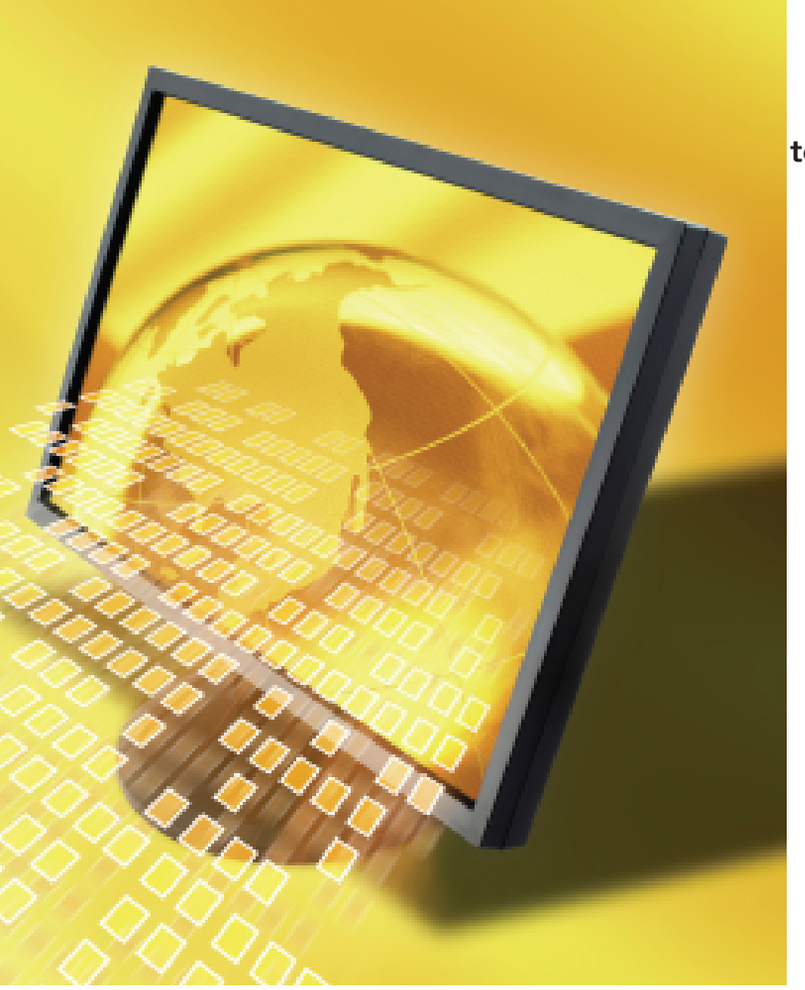
Cash management The solution must accommodate the corporate infrastructure (which may be complex), internal and external forecast data source integration, cash management banking integration, analytical consolidation requirements and time horizon variation.

Accounting The solution must accommodate the company's specific chart of accounts and accounting rule management requirements.

Hedge accounting If the company adopts hedge accounting, the technology solution must accommodate the more detailed interpretations of both FAS 133 *Accounting for Derivative Instruments and Hedging Activities* and IAS 39 *Financial Instruments: Recognition and Measurement* demanded by some auditors – and which are likely to change.

Risk management This is another area where individual treasurers' policies (and preferences) need to be accommodated. The topic is vast, and extends from counterparty exposure limit management and mark-to-market revaluation to higher-end requirements such as value at risk derivation and scenario analysis.

Another area where a standard ASP solution may fall short is instrument coverage. Treasurers tend to underestimate the demands that certain instruments make on technology. Examples include bank guarantees, money market fund investments and withdrawals, letters of credit, performance bonds, non-standard interest rate swaps, securitisation programmes and exotic currency exposures. Any contemplated technology solution should be tested against the requirements of these instruments.



A LEGITIMATE ASP USER MODEL An ASP solution will work for a treasury that fits the standard model of straightforward reporting, processing and instrument requirements – and especially of minimal interfacing – as discussed above. The solution needs to be clearly defined and (at least, relatively) generic, and to be satisfactorily resolved by the ASP system's capabilities.

An entry-level treasury that fulfils these criteria may achieve the following benefits from an ASP:

- ASP offers an accelerated implementation time, as the standard technical setup is performed by the vendor. This is of particular value to companies undergoing corporate events such as a spin-off, and are working to very demanding project timelines;
- The contractual basis of ASP services typically provides a high degree of flexibility; some contracts may even be cancellable on as little as one month's notice. ASP can therefore serve as a stepping stone – for example, as an initial step into treasury technology for a company that is enjoying explosive growth;
- The subscription pricing usually associated with ASP enables companies that need to avoid capital expenditure to deploy treasury technology in a cost-effective way;
- Companies whose policy includes the outsourcing of non-core activities will see treasury ASP services as a route to outsourcing treasury technology. And there are some instances in which treasurers prefer to deal with a third party such as an ASP provider as opposed to the in-house IT department. IT departments may regard treasury as an isolated, specialist function beyond the scope of enterprise systems, and suitable for ASP resolution;
- Arguably, the use of an ASP transfers a proportion of the treasury's operational risk from the company to the ASP provider.

IMPLICATIONS There are some practical aspects of running an ASP solution that may not be apparent in the evaluation process. A particular nuisance factor arises in the kind of shared environment set out in *Figure 1*: all users will be required to upgrade simultaneously when the vendor decides to implement a new release of its system. This has many implications for the prudent treasurer, including the advisability of evaluating the vendor's version control methodology when the solution involves, for example, the sharing of an application server. Upgrades bring the necessary extra workload of testing the new version, to ensure that results are accurate and that reports, interfaces and treasury processes all operate correctly.

So the picture that emerges for entry-level treasuries is that their requirements should fit the ASP solution's standard model of functionality, integration and reporting as closely as possible. Their needs should include limited integration and configuration flexibility, and they should verify that their STP aspirations can be properly met by the proposed solution. The business model that suits ASP vendors is one of stability and uniformity, as standard delivery process and substance should minimise their costs. This tends to be incompatible with the requirements of relatively complex treasuries such as multiple ERP and bank interfaces, and individually demanding requirements, such as regression analysis in hedge accounting.

Nor might ASP suit companies with a global network of treasury centres, unless the vendor offers 24/7 uptime and support coverage in the required time-zones and languages. It is certain that the provision of such extended services will be relatively expensive.

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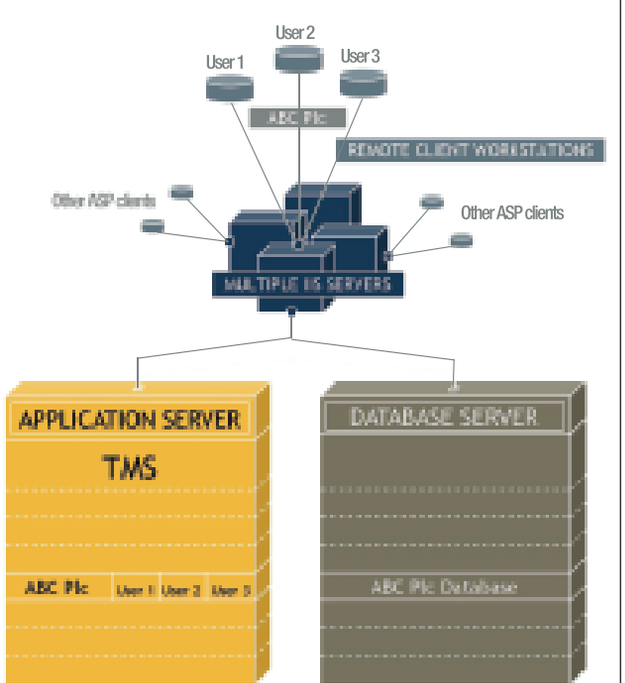
The December issue will contain the second half of this article: the implications of ASP technical delivery for the treasurer.

Figure 1: Generalised ASP technology



Remote client workstations: The means by which ASP users access the system using their web browsers to communicate transactions, initiate system actions and receive reports.
Internet information server (IIS): The machine that controls the internet-based intercommunication between the remote users and the TMS running on the application server.
Application server: A powerful, fast machine that can support multiple users of many ASP clients. This is where the TMS actually runs. Each partition is analogous to a client in a client/server arrangement.
Database server: A machine that manages the databases of the ASP clients.