

# XBRL FILING: New options for Mutual Fund managers

*The purpose of this whitepaper is twofold: to help mutual fund professionals understand the significance of the Securities and Exchange Commission's XBRL filing initiatives, and to present the various filing options available in voluntary XBRL programs. It provides a non-technical explanation of XBRL, explores the evolving impact of XBRL on the mutual fund community, and evaluates the merits of four approaches to XBRL filing — from manual to fully automated.*

## Executive Summary

In early 2005, the Securities and Exchange Commission (SEC) launched an initiative which allowed publicly traded companies to file financial reports on EDGAR using XBRL. XBRL — which stands for Extensible Business Reporting Language — is an XML-based computer language specifically created for automating business information requirements such as the preparation, sharing, and analysis of financial reports. In August of 2005, the SEC expanded the XBRL voluntary filing program to allow mutual funds to use it for filing certain financial reports electronically. However as of this date, only one mutual fund company has chosen to participate in the program. The industry's reluctance may be understandable.

According to the Investment Company Institute (ICI) financial reports provide important disclosures to investors in evaluating individual securities. But that information is not as valuable to mutual fund shareholders. "The current XBRL tagging system for mutual funds principally focuses on financial statements," ICI president Paul Schott Stevens told the SEC Interactive Roundtable in June of this year. "For operating companies, these financials contain most of the information shareholders want. But for mutual fund investors, financial statements are of secondary importance."

Stevens argues that by contrast, for almost a decade under the SEC's disclosure rules, the Risk/Return Summary contained in a mutual fund prospectus, has highlighted the crucial information that investors use in deciding which funds to buy. Risk/Return prospectus summaries provide such key information as fees, expenses, historical performance and risk characteristics of a mutual fund.

In June of 2006, the ICI announced its plan to lead an industry-wide initiative to support voluntary XBRL filings of Risk/Return prospectus summary information with the SEC. In January of 2007, the ICI released its version of the Risk/Return taxonomy. The SEC is currently considering a Risk/Return extended voluntary filing rule (File Number: S7-05-07). In preparation for that rule, the ICI has announced an Education Series for its members to educate on the voluntary filing program. The first training session is scheduled for May 22 in Boston. When the SEC begins accepting such filings (possibly as soon as 2nd quarter 2007), mutual fund administrators and accounting professionals will need to decide whether to participate in the voluntary program and if so, how to convert their information into the proper XBRL file output.

They will have four main options for preparing (tagging) data for XBRL transmission: 1) Tag it manually using a third-party software package; 2) Outsource to a third party, such as a printing company; 3) Use a content management system with XBRL capabilities; or 4) Repurpose validated data from a performance or financial reporting data repository with XBRL capabilities. In exploring these options, mutual fund companies need to consider which solution offers the greatest accuracy, timeliness, and scalability — particularly as more funds and filing options are added over time.

## XBRL Basics

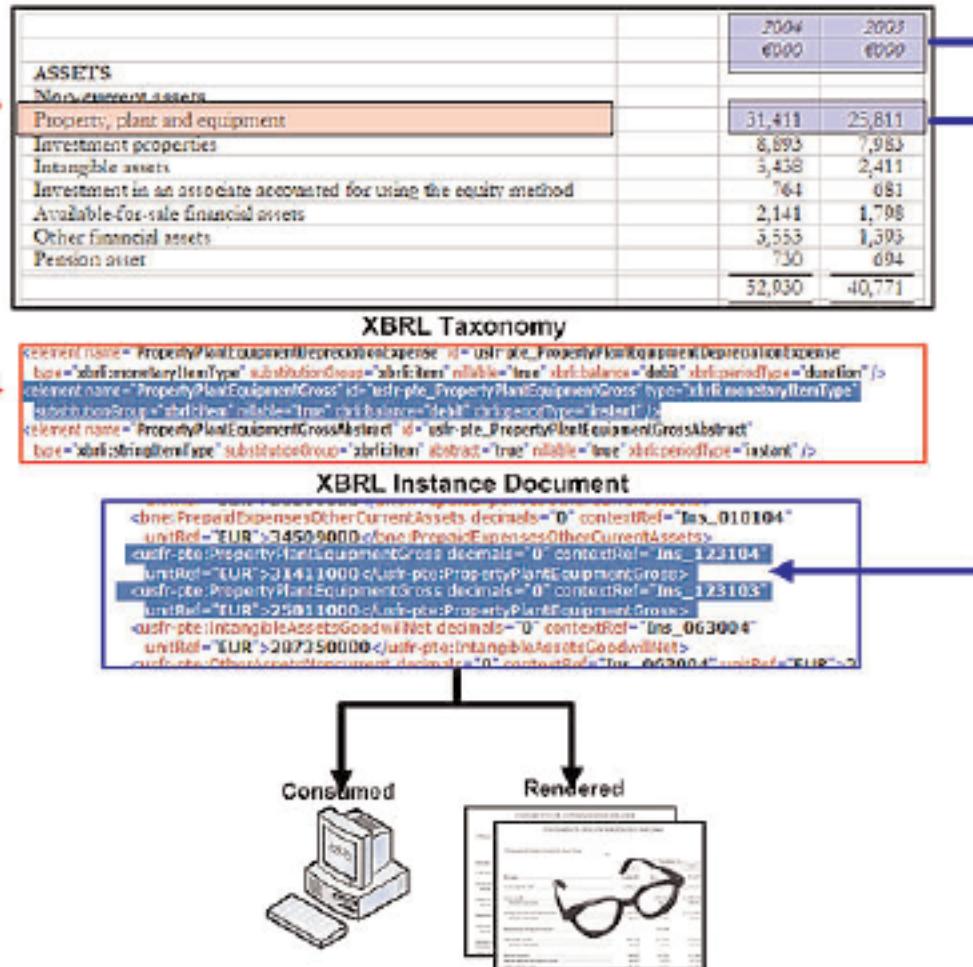
XBRL is a language for the electronic communication of business and financial data. XBRL stands for eXtensible Business Reporting Language. It is one of a family of "XML" languages which are becoming the standards for communicating information between businesses and over the Internet. The goal of XBRL is to save costs, improve efficiency, increase accuracy and enhance reliability to anyone supplying or using financial data on the Internet. In essence, XBRL translates the language of accounting into computer language. Instead of treating financial information as a block of text, such as a standard Internet page or a printed document, XBRL provides an identifying "tag" for each data element. For example, in a corporate financial statement "net income" would have its own tag. These tags are computer readable.

XBRL "taxonomies" are the dictionaries the language uses. They represent categorization schemes that define specific tags for individual items of data (such as "net income"). Custom taxonomies may be developed for specific industries or business applications, including financial reporting.

## How It Works

XBRL is an XML based taxonomy with which users can prepare, publish, exchange and analyze financial statements and the information they contain. An XBRL Instance Document is a business report, such as a financial statement, prepared to the XBRL specification. The meaning of each value in the Instance Document is explained by the taxonomy. An XBRL-enabled computer application will read this information, compare it to a published XBRL definition, and extract the information accordingly.<sup>1</sup>

### Statement of Financial Position



Source: [http://www.ey.com/global/content.nsf/International/XBRL-What\\_is\\_XBRL](http://www.ey.com/global/content.nsf/International/XBRL-What_is_XBRL)

## XBRL for Mutual Fund Companies

XBRL dates back to 1998 when a CPA in Tacoma, Washington began developing prototypes of financial statements and audit schedules using XML. However, it wasn't until early 2005 that the SEC established a voluntary program for publicly traded companies to report financial information on EDGAR using XBRL. Later that year they expanded the XBRL voluntary filing program to allow mutual funds to file certain reports in XBRL.

Right now, 24 companies are participating in the SEC's XBRL voluntary filing program, but only one is a mutual fund company. One reason for the lackluster success of the voluntary mutual fund financial reporting XBRL program may be that shareholders already have access to a plethora of mutual fund data sources online, including third-party services and mutual fund company Web sites. Another reason may lie in the fact that the filings have focused on financial reporting data rather than risk and return information. In a 2006 survey of mutual fund shareholders, ICI found that the top three types of information mutual fund buyers reviewed before making a purchase were: Fees and expenses (74 percent), historical performance (69 percent), and fund risks (61 percent)<sup>2</sup>. These items are included in the beginning of the prospectus in the Risk/Return Summary.

Accordingly, the ICI is leading an initiative to augment XBRL filings so that mutual funds can provide XBRL filings of Risk/Return Summary information. To help develop the new Risk/Return taxonomy, the ICI engaged PriceWaterhouseCoopers and created a working group including ICI members and XBRL stakeholders. The project, which was launched on June 12, 2006, plans to have an initial version of the taxonomy by mid-September 2006 with the final version expected by early 2007. The ICI will encourage members to file voluntarily using the new XBRL Risk/Return taxonomy via EDGAR.

More evidence of the SEC's commitment to XBRL came in August of this year when it announced plans to provide its own Web tools to let investors and analysts exploit interactive data for analysis of mutual fund and corporate information. At the same time, they solicited a proposal for the development of web-based analysis software that would allow investors and analysts to use interactive data encoded in XBRL.

## EDGAR and XBRL Filings: Understanding the Difference

Preparing an XBRL filing is different than preparing a current EDGAR filing. EDGAR filings are supported by HTML which is used to **format** information into headings, paragraphs, lists and so on. XBRL, on the other hand, is used to tag the **meaning** of specific financial reporting data elements. For example, a specific XBRL tag would be assigned to represent "net income". So unlike HTML, XBRL requires the user to understand the elements of a financial statement in order to make sure the data is accurately tagged.

## Calling All Volunteers

So far, mutual fund XBRL filings are completely voluntary. Fund companies may choose to file voluntarily for a variety of reasons. For example, they may use it to create competitive differentiation by demonstrating openness, transparency, and a commitment to empowering their investors to make better-informed decisions. Or, if they believe the SEC will eventually make XBRL mandatory, they may decide to participate in order to gain a working knowledge of the system before they are required to do so.

But regardless of whether a fund company decides to participate in the Risk/Return Summary pilot project, it is important to understand that both the SEC and the ICI have embraced the concept of "interactive data" and see the Internet as the new frontier for shareholder disclosure. According to the SEC, interactive data means using technology to provide investors with quicker access to the information they want, in a format they can use. Interactive data points include all of the facts and figures trapped in dense documents.

This flexible format allows investors to quickly pull out the information they want and compare it to the results of other companies, to performance in past years, to industry averages — essentially any way the investor wants to slice and dice the data. Beyond that, the SEC believes XBRL data tagging will enable them to review filings more efficiently.

Securities and Exchange Chairman Christopher Cox has made the use of information technology and the Internet a priority for improving the quality, timeliness, and usefulness of disclosure for individual investors. He has claimed that effective use of available technology will "change the game for millions of ordinary investors."<sup>3</sup>

ICI research supports the SEC's stance. ICI president Paul Schott Stevens acknowledged before the SEC Interactive Data Roundtable in June of this year that the time is right to seize the Internet's potential to better inform investors. Their survey found that 88 percent of U.S. fund investors now have access to the Internet — up from 68 percent in 2000 — and that most of them use it regularly, including for financial purposes.<sup>4</sup>

## About Risk/Return Summary Filing

The taxonomy being developed by the ICI is expected to cover the Risk/Return Summaries contained in all mutual fund prospectuses, including:

- the fund's investment objectives/goals
- the fund's principal investment strategies
- the principal risks of investing in the fund, including a narrative description of these risks and graphic presentations of historical performance
- the fund's standardized fee table

This Risk/Return information represents items 1–3 of the SEC Form N-1A, which are designed to provide investors with information to help them make decisions about investing in mutual funds.

Specifically, the elements of the Risk/Return Summary in the custom taxonomy include:

### **Part A Item 1: Front Back Covers**

The front and back cover pages include fund objectives, operations, and how more information about the fund can be obtained from the Statement of Additional Information (SAI).

### **Part A Item 2: Investments, Risks, and Performance**

This section begins with the fund's objective and goals, its investment strategies, and a narrative risk disclosure. It shows the Risk/Return bar chart and table which are meant to display investment risk by providing a fund's performance from year to year and by comparing the fund's average annual returns for 1, 5, and 10 years with broad measures of market performance.

### **Part A Item 3: Fee Table**

This section discloses the fees and expenses a shareholder would pay if they bought shares of the fund. It shows a chart which outlines the fees paid directly from the investment, such as front and back end loads or redemption fees. It also displays the percentage of annual operating expenses deducted from the fund's assets. Finally, the fee table provides an expense example which calculates total expenses on the fund's loads and fees for a hypothetical \$10,000 investment with a 5 percent return each year.

## **Evaluating Your Options**

Assuming your fund company chooses to participate in the Risk/Return Summary voluntary filing project, the next step is determining how to file. "Even after the Risk/Return Summary taxonomy is implemented, the number of funds in each complex increases the challenges involved in making sure that fund companies and their service providers can tag data accurately and efficiently in an ongoing manner."<sup>5</sup>

Participants in the SEC voluntary XBRL filings have four main options for preparing (tagging) data for XBRL transmission: 1) Tag it manually using a third-party software package, 2) Outsource to a third party, such as a printing company, 3) Use a content management system with XBRL capabilities, or 4) Repurpose validated data from a performance or financial reporting data repository with XBRL capabilities.

These four options, as they apply to the pending Risk/Return Summary XBRL filing program, are as follows:

1. **Manual tagging** — A number of third-party software packages are available to help businesses prepare financial reporting filings. With third-party software, fund companies would enlist their own employees to manually tag the data within the classifications defined in the taxonomy. The most obvious drawback of this approach is that it would require many hours of staff time — and those demands on staff would multiply with the addition of new funds and reporting requirements. Beyond that this approach relies on error-prone manual input of data into an XBRL tagging software system. It also assumes that the data provided for input is correct in the first place, a risky assumption when it was originally calculated using spreadsheets or manual processes.
2. **Outsource** — Fund companies have a number of outsourcing options to support XBRL, including the accounting firms which handle their financial data and firms that print their financial reports. The benefit of outsourcing is that, because someone else is doing it for you, you avoid any potential impact on staff resources. One downside, though, is that the creation of XBRL files still relies on error-prone manual data input, which puts the integrity of the data at risk. This approach shares with the manual input option its assumption that the data is correct in the first place. Another downside to outsourcing is the loss of control over the XBRL data tagging process and the risk of erroneously classifying financial data elements incorrectly, which could also prove to be very serious.

"Even after the Risk/Return Summary taxonomy is implemented, the number of funds in each complex increases the challenges involved in making sure that fund companies and their service providers can tag data accurately and efficiently in an ongoing manner."<sup>5</sup>

**Paul Schott Stevens**  
**President of the ICI**

"... because XBRL offers a way to integrate disparate forms of financial data simply by tagging them with standardized code, companies may find that any number of software companies and related service providers are only too happy to offer the capability at little or no charge."<sup>6</sup>

CFO, August 2006

3. **Content Management Systems** — A content management system automatically identifies data within the document and streamlines its flow from one review point to the next.

Its principal advantage is that it usually provides better tagging results since the data is identified within the system. The most apparent downside of this approach is that content management systems rely on the accuracy of data manually entered into the system, particularly when the data was calculated from source systems and/or spreadsheets.

4. **Repurpose validated source data** — The most accurate option for Risk/Return Summary XBRL reporting is to repurpose data which has already been calculated and validated. The main advantage is data integrity; you are assured that all performance calculations are validated for accuracy and you eliminate the risk of manual errors. The system automates the mapping of your data to the XBRL taxonomy and ensures that the same data which appears in your prospectus goes straight through to the SEC. This solution is also highly scalable, which means that additional funds and XBRL reporting demands can be added without increasing staff.

While it is too early to be sure, cost does not appear to be a primary factor in selecting an XBRL option. A recent article in CFO magazine entitled "XBR- What?" noted: "Because XBRL offers a way to integrate disparate forms of financial data simply by tagging them with standardized code, companies may find that any number of software companies and related service providers are only too happy to offer the capability at little or no charge."<sup>6</sup> In effect, the key decision criteria come down to these: the level of automation, the accuracy of the XBRL data filing, timeliness of the filing, and scalability of the solution to accommodate additional funds and reporting requirements without impacting staff levels.

## Options for Preparing Your Risk/Return Summary XBRL Filing

XBRL Tagging Options	Level of Automation	Accuracy	Timeliness of Data	Scalability
Manually using third-party software	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
Outsource to a third party	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
Directly from a financial reporting content management system	<input checked="" type="radio"/>	<input checked="" type="radio"/>	<input checked="" type="radio"/>	<input checked="" type="radio"/>
Directly from the data source	<input checked="" type="radio"/>	<input checked="" type="radio"/>	<input checked="" type="radio"/>	<input checked="" type="radio"/>

Low:  Moderate:  High:

## Conclusion

While currently voluntary, XBRL filing of mutual fund information to the SEC has the potential to become the new standard for shareholder disclosure. Astute mutual fund administrators and tax accounting professionals are following the progress of XBRL with a watchful eye. Not only must they make strategic decisions regarding their participation in the voluntary filings, they must also decide what strategy will best enable them to actually file data with the SEC using XBRL. Key decision factors include the inherent risk of error due to manual processes, the timeliness of the XBRL transmission, and the scalability of the solution to meet growing demands for additional XBRL data filings over time.

## Definitions

**XML** — XML stands for the Extensible Markup Language. It is intended to improve the functionality of the Internet by identifying information in a more accurate, flexible, and adaptable way. It is extensible because it is not a fixed format like HTML (which is a single, predefined markup language). Instead, XML is actually a meta-language—a language for describing other languages—which lets users design their own markup languages for different types of documents.

**XBRL** — XBRL stands for eXtensible Business Reporting Language. It is a language for the electronic communication of business and financial data. It is one of a family of XML languages which are becoming the standards for communicating information between businesses and across the Internet.

**Tagging** — XBRL provides an identifying “tag” for each type of data. For example, in a corporate financial statement “net income” would have its own tag. The tags are computer readable.

**Taxonomy** — a “vocabulary” or “dictionary” created by a group of users to exchange information. For example, XBRL taxonomies exist for International Financial Reporting Standards (IFRS) and United States Generally Accepted Accounting Standards (US GAAP).

## About Confluence

Confluence, the global investment management industry's leading provider of fully automated data management solutions, offers investment management firms a comprehensive fund administration platform designed to reduce costs and eliminate risk through automation and the consolidation of critical business processes. The platform features FundStation® for performance measurement and Clear Portfolio™ for holdings and financial statement reporting. Confluence products and reporting services automate every step of the process—collection, creation, confirmation and delivery—for investment product data. Over 60 percent of U.S. mutual funds rely on Confluence to solve a wide range of problems. Major investment firms such as Merrill Lynch, Franklin Templeton and Janus, as well as service providers such as PFPC, BISYS, The Bank of New York and U.S. Bancorp, all leverage Confluence solutions.

**April 23, 2007**

1 [http://www.ey.com/global/content.nsf/International/XBRL-What\\_is\\_XBRL](http://www.ey.com/global/content.nsf/International/XBRL-What_is_XBRL)

2 Source: Investment Company Institute, Understanding Investor Preferences for Mutual Fund Information, 2006  
[http://www.ici.org/home/rpt\\_06\\_inv\\_prefs\\_full.pdf](http://www.ici.org/home/rpt_06_inv_prefs_full.pdf)

3 Speech by SEC Chairman: Opening Remarks to the Practicing Law Institute's SEC Speaks Series, March 3, 2006.

4 Source: Investment Company Institute, Mutual Fund Shareholders' Use of the Internet, 2005

5 Speech by Paul Schott Stevens before an SEC Interactive Data Roundtable, June 12, 2006

6 XBR-What? CFO Magazine, August 01, 2006