

CASTLE HALL
ALTERNATIVES

The Due Diligence Company

Operational Due Diligence

Institute of Managed Account
Professionals
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External Manager Risk

Investment Risk

- ▶ Risk of loss due to the execution of the investment strategy: unprofitable trading

Operational Risk

- ▶ Deliberate theft and fraud – Madoff, AIJ
- ▶ Errors in accounting / NAV calculation
- ▶ Weak business infrastructure: poor management, inadequate resources. In this context, Operational Risk is a subset of broader **Business Risk**

The Scope of ODD

Management Company

- ▶ The “Business Risk” of the management company

Fund

- ▶ The “Legal Risk” of the fund

Controls

- ▶ The “Operational Risk” of the control environment

The Scope of ODD - Detail

BUSINESS RISK

The Manager

- Management company
- Principals and key professionals
- Ownership
- Assets under management
- Insider investment
- Human resources
- Regulation oversight
- Compliance infrastructure
- Information technology

LEGAL RISK

The Fund

- Corporate structure
- Service providers
- Corporate governance
- Terms of investment
- Fees and expenses

OPERATIONAL RISK

Control Environment

- Prime brokers, custodians and counterparties
- Asset transfers
- Trading controls
- Valuation controls
- Net asset value controls
- Financial reporting controls
- Manager transparency
- Operational due diligence (Fund of funds)

The Due Diligence Workflow



Screen

- ▶ Initial due diligence to validate potential manager allocation

Onboard

- ▶ Detailed due diligence prior to investment

Monitor

- ▶ Ongoing due diligence to identify, evaluate and action changes in operational and business risk factors

ODD for Managed Accounts

- ▶ Allocating to a manager who undergoes an operational issue can be organizationally burdensome and have a material impact on the allocator – even if capital is eventually recovered. Franchise risk?
- ▶ Regulatory requirements in Australia
- ▶ Industry expectations
- ▶ Differentiation – smaller managers may provide differentiated investment strategies, but can introduce elevated manager specific risk. Does a manager have an “I told you so” weakness?
- ▶ International managers – allocation directly to non Aus fund structures; or allocation via an Aus trust which then feeds into an international structure (regulated jurisdiction such as Ireland / Luxembourg, non regulated such as Cayman)

Presentors



The Due Diligence Company



CHRIS ADDY, CEO - CPA, CA FCA CFA

Chris is one of the industry's very first ODD professionals, beginning his due diligence career in 1997 with The Atlantic Philanthropies (\$5bn foundation and early hedge fund investor). He then joined UBP (2001) and cofounded Amber Partners (2004). Prior to forming Castle Hall, Chris' experience covered due diligence from the perspective of an institutional investor, a fund of funds, and a manager-focused consultant.

External to Castle Hall, Chris is a member (and prior chair) of the CFA Institute Capital Markets Policy Council and is a founding member of the Executive Committee of the Fund Governance Association.



ALEX WISE, EXECUTIVE CONSULTANT ASIA PACIFIC - LLB, BVC, QLTT

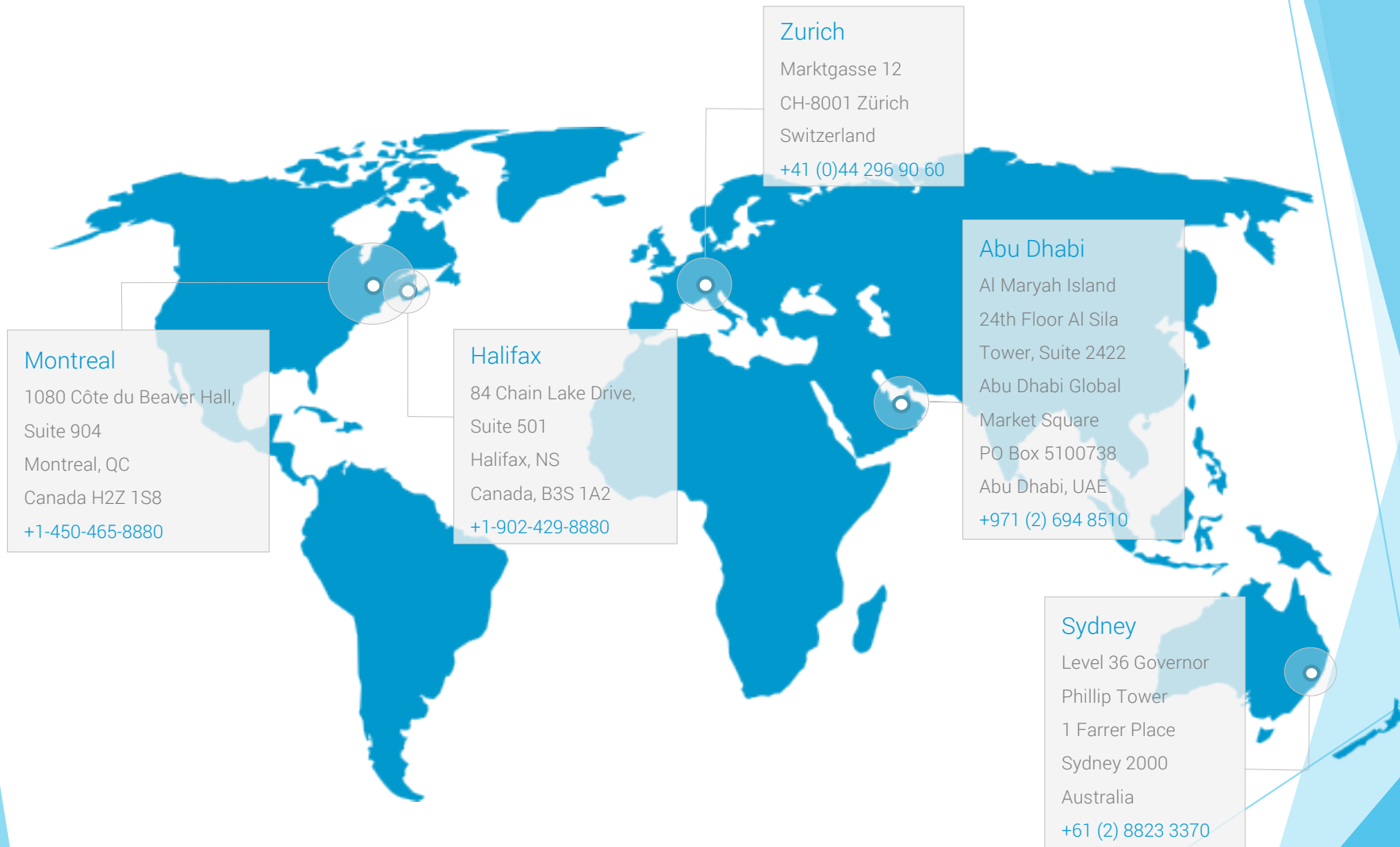
Alex is supporting Castle Hall's client relationships and diligence activities in Australia and the broader Asia Pacific region. Alex has 12 years' experience in the hedge fund industry and prior to that worked in a leading London law firm. Alex established the operational due diligence program at Atlas Capital, a UK / Guernsey based fund of funds, in 2002, before moving to found Orchard Harbour, a leading specialist in Asia-Pacific hedge funds, in 2007. Alex is a qualified Solicitor and a Barrister in England & Wales having completed the Bar at the College of Law in London. Alex is also an executive committee member of AIMA's Australian chapter.

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