



AIMA Due Diligence Considerations for Retail Investment Advisors: Hedge Funds, Alternative Mutual Funds & ETFs, Private Credit Funds

INVESTMENT MANAGER

- What is the background and experience of investment manager & the investment team?
- What is the governance surrounding the investment manager & investment team?
- What are the features of the investment manager's compliance culture?
- What risk management frameworks are in place? For example, independent reporting lines, operational risk management, conflicts of interest, relationship disclosures, etc.?
- Are the members of senior management of the investment manager, the portfolio manager and/or the fund directors personally invested in the fund?

STRATEGY

- What is the fund's investment objective and principal investment strategies?
- Have the objectives of the investment strategy changed in the past 5 years?
- From where are the underlying positional data, market data and any underlying models sourced for this strategy?
- Are there position limits and what are they?
- Who makes the portfolio management decisions and how are they made?
- What is the performance history? In what type of markets would this strategy be expected to outperform or underperform?
- What method(s) does the investment manager use to measure the total risk of a portfolio using this strategy?
- How much financial leverage does the fund use on average? What are the limits? What are the sources of leverage?
- Are there any capacity constraints?
- Offering documents, subscription agreements, and process for purchases and redemptions?
- What are the fees, including performance fees and calculation methodology?
- What is the valuation policy and frequency of valuation?
- How long would it take in normal market conditions and stressed market conditions to liquidate the fund without incurring unusual costs?
- What level of transparency and portfolio data does the investment manager provide to investors, and with what frequency and time lag?

- Who are the outsourced service providers of the fund? For example, prime broker, auditor, custodian, administrator, legal counsel, etc.?

PRIVATE CREDIT STRATEGY

- How does the investment manager source potential borrowers? Direct relationships with the borrower (e.g. in-house advisory), private equity sponsors, banks, via corporate debt advisors (e.g. audit firms/lawyers, consultants etc.), marketplace lending platforms?
- What is the typical target range of maturities sought?
- How are repayment terms on originated loans typically structured?
- Describe the investment manager's credit assessment and due diligence process.
- What types of representations, warranties and covenants are the borrowers required to give and what collateral is required? How is this monitored?
- What is the investment manager's policy towards impaired/stressed loans or bad debts and what track record does they have?

Alternative KYP Comparison – CSA Client Focused Reforms

In 2021, the CSA (Canadian Securities Administrators) implemented amendments to NI 31-103, the [Client Focused Reforms](#) (CFR). This enhanced the documentation of work required with regards to KYP (Know Your Product), KYC (Know Your Client), fund suitability and monitoring of material changes to funds.

Dealers and advisors have implemented various processes and technology solutions in order to better meet CFR requirements based on their diverse interpretations of this principles-based legislation.

AIMA encourages dealers and advisors to ensure their KYP processes are robust and compare across a wide array of metrics and beyond funds in the same CIFSC (Canadian Investment Funds Standards Committee) category, as there may be alternative funds investing in the same universe or sector that provide improved risk/return metrics vs long-only peers.

For example, the Alternative Equity Focused category might have funds that could be contrasted with Canadian Equity category, Canadian Neutral Balanced, Global Neutral Balanced or more.

Beyond the initial risk/return metrics (fees, 1-year return, 3-year return and standard deviation) in KYP comparisons, AIMA encourages dealers and advisors to consider further risk metrics: Maximum Drawdown & Time to Recovery, Sharpe Ratio, Correlation, Up/Down Capture, Sortino Ratio, Alpha, Beta, Batting Average, (Conditional) Value at Risk, amongst others.

July 2022