



# AIMA Canada's Hedge Fund Investor Checklist

## Note on Using The Checklist:

- This checklist is designed for you, the investor, to use once you and your financial advisor have determined that an allocation to hedge funds is suitable for your portfolio, given your overall investment objective.
  - This *basic* checklist focuses on the key practical issues you should consider prior to investing in any specific hedge fund product. It is not designed to be an all-encompassing checklist.
  - You should consult with your financial advisor when using this checklist. Also, you may wish to consult with your professional legal and tax advisors for specific legal and tax questions.
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## 1. Due Diligence

- Is there a qualified individual or team that evaluates hedge funds and principal protected notes for your financial advisor?
- What specific issues are assessed in the due diligence process? What is the depth and quality of the assessment? How often is the product assessed?
- Has the product issuer completed AIMA's due diligence questionnaire for hedge funds or hedge fund-of-funds as part of the due diligence process?

## 2. Manager and Organization

- What relevant hedge fund experience does the hedge fund or hedge fund-of-funds manager have?
- What other experience, qualifications and registration does the hedge fund or hedge fund-of-funds manager have?
- What is the depth and quality of the hedge fund manager's corporate business infrastructure, including staffing, and what is the hedge fund firm's capital structure? Is it a viable business?

## 3. Strategies and Risks

- What type of hedge fund product are you investing in (i.e., a single-strategy, single-manager hedge fund or a multi-strategy, multi-manager hedge fund-of-funds)?
- Do you understand the hedge fund's investment objective, how the strategy works and how the manager generates returns?
- Do you clearly understand the key risks associated with the hedge fund investment? Specifically:
  - What is the fund's volatility of returns, leverage risk, concentration risk, market risk, and liquidity risk?
  - What has been the fund's maximum drawdown (loss) and in what circumstances did this occur?

## 4. Performance

- How are the hedge fund returns presented (i.e., are they actual returns or pro-forma returns)?
- Are the hedge fund returns stated gross or net of all fees?
- How do the risks and returns of the hedge fund product compare to other similar hedge fund products?
  - If the product outperformed other similar products, how was this achieved? For example, was leverage used?

## 5. Liquidity

- How often can you redeem the hedge fund investment?
- Does the hedge fund product have any redemption restrictions (i.e., lock-up periods, notice period, redemption fees)?

## 6. Fees and Commissions

- Is the hedge fund's fee structure clearly disclosed? Do you understand the mechanics of the fee structure?
- What compensation will your financial advisor receive for selling the hedge fund product? Is this compensation consistent with similar products?
- Do you understand who is being compensated, when and how much?

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## 7. Taxes

- Are there any distributions from the hedge fund investment? If so, how are they taxed (i.e., income versus capital gains, or both)?
- How will the hedge fund investment be taxed upon redemption (i.e., income or capital gains)?

## 8. Principal Protected Notes ("Notes")

*The following are additional questions that should be considered for principal protected hedge fund notes (i.e., where the principal is guaranteed at maturity).*

- Can you redeem the Note prior to maturity?
  - Is there a secondary market for the Note?
  - Who will make the secondary market for the Note?
- What are the tax consequences for selling the Note prior to maturity?
- What is the cost for principal protection? Is this cost clearly disclosed?
- Who is the guarantor providing the principal protection? Is the guarantor a reputable financial institution with a good credit rating (i.e., AA or better)?
- What type of hedge fund is the Note based on (i.e., a single-manager, single-strategy hedge fund or a multi-strategy, multi-manager hedge fund-of-funds)?
- If it is a hedge fund-of-funds, is it diversified or concentrated in a particular strategy? Is leverage used? If so, how much and by whom?
- Do you understand under what circumstances the Note may be invested only in zero-coupon bonds until maturity, with no exposure to the underlying hedge fund?

## 9. Offering Documents

- Has your financial advisor read the key reference document for the hedge fund product, whether a prospectus, offering memorandum or information statement?
  - Have you received and read the key reference document for the hedge fund product?
  - Can your financial advisor provide you with reasonable explanations for any items that are unclear or you are concerned about?

## 10. Other Issues

- Have you asked your financial advisor about all of the issues relating to the specific hedge fund product that may be unclear?

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### Additional Information and Notes

- For additional information on hedge funds, please see the *AIMA Canada Hedge Fund Primer*, available on the AIMA Canada website at [www.aima-canada.org](http://www.aima-canada.org).
- This checklist is to be included in the *Best Practices Manual* published by Advocis, The Financial Advisors Association of Canada. Advocis has included this checklist in its compilation of industry practice management tools for financial advisors.

### AIMA Disclaimer

- AIMA Canada is the Canadian Chapter of the Alternative Investment Management Association (AIMA).
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