

Selecting a candidate: due diligence — what to look for, what to ask

Dermot Butler of Custom House gives some guidance on how to pick the perfect administration candidate – and explains why detail that is missing from a reference is as important as what is included

It is extraordinary to me that many prospective managers still do not carry out even basic due diligence when selecting a candidate, other than getting a fee quote.

Let me be quite categorical – due diligence is essential when choosing a candidate.

To do this, ask the prospective candidate (the “candidate”) to complete a detailed questionnaire. In this context, it is worth noting that AIMA – the Alternative Investment Management Association – has published a series of guidelines for due diligence questionnaires, including one for candidates and I suggest using this questionnaire for each candidate.

I would also suggest reviewing the AIMA Guide to Sound Practices for Hedge Fund Candidates and then ask candidates if they comply with those guidelines.

If, having reviewed the completed questionnaire (remember the questionnaire is an elimination tool, not a selection tool), the manager decides that a candidate is still in the running, then he should carry out further checks, including, inter alia:

- Get references and be clear about what the references say – and what they don't say.

I have told this story before, but I think it bears repeating. When I first moved to Ireland, I was looking for someone to work at my home. My lawyer at the time, who was a canny old bird, told me to look out for what was missing from a reference – what was written may not

be quite so relevant as what was not.

For example, if the reference didn't say that the person I was considering employing was sober and honest, then that probably meant that he was a drunken thief.

Look for similar clues.

- Look at more than one candidate – hold a beauty parade – find out what they offer.

- If practical, which is not always the case, visit their offices and see what they do and how they do it.

- Quite soon, it will be clear whether they are able to offer a personal service and which candidate will allocate one named person as the account executive (with named backed up). The personal approach is very valuable.

- Ask the candidate how many clients they have in total and how many invest in the same asset classes, sectors or disciplines as the Manager.

If dealing in an exotic instrument, and the candidate has never handled that instrument, then the manager must ensure that it is capable of doing so.

- Review the Candidate's standard agreement and get a detailed procedure manual to explain exactly what the candidate is going to do and – very important – who is responsible, in which office, for each specific task.

- Find out the qualifications of the candidates' staff - how many

professionals do they have – previous employment history etc. – but, remember, experience is often more valuable than initials after the name.

- Can the candidate handle equalisation? Do they do this on a manual spreadsheet or is it automated and integrated into their main system? The answers to the due diligence questionnaires, combined with the visits and other recommendations that I have made, should enable the Manager to select the winner of the beauty parade.

Having made the selection, don't go for the cheapest, go for value.

Remember, a candidate should add value to a fund, and the more the candidate is asked to do, then the more it will cost.

Many managers assume that administration is a simple bookkeeping task and that the candidate that can do it cheapest, is the one. Rest assured that this is likely to be a totally false economy.

It's an old cliché, but if you pay peanuts, you get monkeys. ■

