STANDARDS BOARD FOR ALTERNATIVE INVESTMENTS

Broker-Dealer Products

Alternative Risk Premia Due

Diligence Questionnaire (DDQ)

This document contains the Due Diligence Questionnaire institutional investors and asset managers can use to assess broker-dealer products. It was developed by the SBAI’s Alternative Risk Premia Working Group in collaboration with broker-dealers. More information is available at <https://www.sbai.org/toolbox/alternative-risk-premia/>.

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| **1** | **Experience** |
| 1.1 | Please describe your background and history in the factor/risk premia space. |  |
| 1.2 | How is the business organised? |  |
| 1.3 | Please provide the AUM history of this business splitting out Smart Beta (long only), Risk Premia and other types of indices. |  |
| 1.4 | Please provide the history of annual numbers of investor mandates for this business. |  |
| 1.5 | Please provide a break-down of AUM by client type. |  |
| **2** | **Research & Development** |
| 2.1 | Please describe the firm’s internal quantitative research capabilities. |  |
| 2.2 | Does the firm have a dedicated quantitative team? If yes, where does this sit within the organisation? |  |
| 2.3 | Does the firm leverage academic research? If yes, please describe how this is used? |  |
| 2.4 | Does the firm leverage third party research? If yes, please describe how this is used? |  |
| 2.5 | Please describe the process to validate a new strategy (and to decommission a strategy) |  |
| 2.6 | Please describe the controls/procedures in place to monitor strategies |  |
| 2.7 | For your flagship strategies, can you show the ratio of live production performance vs simulated performance? Can you share historical back tests? |  |
| 2.8 | How is liquidity considered during strategy development? |  |
| 2.9 | Please describe how you define slippage, i.e. when the price at the time of a signal is different from the price achieved when executing the rebalancing of the index? |  |
| 2.10 | How do you assess, measure and monitor market impact? |  |
| 2.11 | Do you set up capacity limits for your strategies? If so how? |  |
| **3** | **Governance** |
| 3.1 | Please describe any potential conflicts of interest and how are they mitigated? |  |
| *3.2* | *Position Keeping and Trading* |
| 3.2.1 | Who maintains and has access to the front-office position keeping? |  |
| 3.2.2 | How are orders communicated to the execution team? |  |
| 3.2.3 | Are you allowed to internalise trades? If yes, against what type of flow? |  |
| *3.3* | *Benchmark Administration* |
| 3.3.1 | Who is the Benchmark Administrator? |  |
| 3.3.2 | Is the Benchmark Administrator fully independent from the broker-dealer?If no, please describe the relationship |  |
| 3.3.3 | Who performs the oversight function within the Benchmark Administrator? |  |
| *3.4* | *Calculation Agent* |
| 3.4.1 | Who is the Calculation Agent? |  |
| 3.4.2 | If the Calculation Agent is an independent third party to the broker-dealer, are they using any code or infrastructure developed by the Broker-dealer? |  |
| 3.5 | Please describe the segregation in place between the research and structuring teams and the execution and prime brokerage/financing teams of the broker-dealer? |  |
| 3.6 | Do control functions (e.g. Legal, Compliance, Risk Management) have the right of veto over the ability to launch or maintain an index in relation to conflicts of interest? |  |
| 3.7 | Please describe the process for amending or terminating an existing Index? How are existing or past investors in the Index consulted and notified? |  |
| 3.8 | How are discretionary events implemented? Who can exercise discretion at the broker-dealer? |  |
| **4** | **Operational Aspects** |
| 4.1 | Do you provide position level look through reporting? If yes, how frequently and in what format? |  |
| 4.2 | Do you provide bespoke risk management reports? |  |
| 4.3 | Do you provide an online reporting tool? |  |
| 4.4 | Are fact sheets, commentaries produced on a regular basis?If yes, at what frequency? |  |
| 4.5 | Please describe the process to trade baskets of Indices. E.g. Single confirmation or multiple? Process to rebalance the basket over time, is this at the discretion of the investor? Can it be done online? |  |
| 4.6 | Do you provide the ability to include Indices produced by other banks within a given basket? |  |
| 4.7 | What are the available delivery possibilities? E.g. Fund? Certificate? Total Return Swaps? Options? |  |
| **5** | **Trading Set Up** |
| 5.1 | Which trading team is responsible for the hedging of the single strategies (the “Hedging Trading Team”)? |  |
| 5.2 | How is that team related to the other traders for the respective asset classes? What organisation/information barriers are set up to avoid information leak from one team to the next? How is it controlled/monitored? |  |
| 5.3 | What are the compensation arrangements for the “Hedging Trading Team” and “Structurers”? (e.g. as a function of transaction fees, product performance (absolute, relative, desk performance) |  |
| **6** | **Team Set Up** |
| 6.1 | Please provide an organisation chart for the business showing the main functions and senior managers for each. Please include bios for senior managers. |  |
| *6.2* | *Team Composition* |
| 6.2.1 | Please provide the number of Structurers dedicated to the business |  |
| 6.2.2 | Please provide the number of Traders dedicated to the business |  |
| 6.2.3 | Please provide the number of quantitative research analysts dedicated to the business |  |
| 6.2.4 | Please provide the number of (non-quant) research individuals dedicated to the business |  |
| 6.3 | Are all structurers for the product within the same team?If yes, are their roles specialised by asset classIf no, please describe the team structures they sit in |  |
| 6.4 | Please provide details of any departures in the past two years. |  |
| 6.5 | Please provide details about the quantitative research effort supporting the business |  |
| **7** | **Investment Process (Strategy Specific)** |
| 7.1 | Please provide a description of the flagship strategy(ies)? |  |
| 7.2 | Please provide a list of main single strategies, including definitions of these strategies? |  |
| *7.3* | *Portfolio Construction* |
| 7.3.1 | Please describe the principles/philosophies for portfolio construction |  |
| 7.3.2 | How are single strategies selected to be part of a portfolio? |  |
| 7.3.3 | How do you ensure diversification within the portfolio? |  |
| 7.3.4 | What is the turnover of the portfolio? |  |
| 7.4 | How is downside risk management taken into account when designing both single strategies and portfolios? |  |
| *7.5* | *Performance of Relevant Strategy* |
| 7.5.1 | When do you expect the strategy to perform will and when do you expect it be challenged? |  |
| 7.5.2 | Please provide the three largest historical drawdowns along with explanations? |  |
| 7.5.3 | Is there anything significantly different in the current market conditions compared to the backtest which could have an impact on the strategy going forward? |  |
| **8** | **Cost Analysis (Strategy Specific)** |
| 8.1 | Define and disclose each of the fees and costs that are or will impact the performance of the relevant strategies and/or portfolios?* *Include all costs, fees, spreads, bid/offers or any other elements (however named)*
* *Include costs irrelevant of where they occur (e.g. in the index, product, hedging or other transaction)*
* *Costs should include but not be limited to bid/offer, brokerage fees, borrow costs, financing costs, service provider costs (administrator, custodian etc.), and entry/exit costs.*
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| 8.2 | The Bank (and Asset Manager for comparison if relevant) shall provide the track record of each strategy and portfolio net of all fees and costs impacting the investor (= the “Net” track record) |  |
| 8.3 | Provide a second track record assuming that each instrument in each index can be traded at mid-market, without any other costs (i.e. no fee, no brokerage, no borrow etc…) (= the “Gross” track record) |  |
| 8.4 | Show the drag coming from the Net vs Gross track records |  |
| **9** | **Index Design (Strategy Specific)** |
| 9.1 | Can the Index’ value be replicated/calculated based on the information included in the Index Rulebook? If not, what is missing? |  |
| 9.2 | Is the index subject to the provisions of the EUBMR or the ISOCO Principles for Financial Benchmarks? |  |
| 9.3 | Are any prices, parameters used in the Index determined by the Broker-Dealer? If yes, what are the checks and balances in place to mitigate conflict of interests? |  |
| 9.4 | What was the rationale for any amendment made to the Index Rulebook since the original Index version was launched? |  |
| 9.5 | Are any costs impacting the value of the Index not disclosed in the Index Rulebook? |  |
| 9.6 | Are any costs impacting the value of the Index not fixed? If yes, please explain the reason and what controls are in place to mitigate conflicts of interest? |  |
| 9.7 | Please describe the approach to back-testing? (time periods used, out-of-sample testing, correlation analysis between in-sample and out-of-sample data, etc.) |  |
| 9.8 | Is the step-by-step impact of optimisations (as set out by Rule Book) on risk and return characteristics of the strategy disclosed? |  |