

NOT JUST ANOTHER TICK IN A BOX: A NEW APPROACH TO OPERATIONAL DUE DILIGENCE

Type 'due diligence' into Google and in less than half a second, 94 million results appear. For 'operational due diligence' (ODD), the results decrease by 99.7%

ODD provides a risk assessment of the internal controls, operations, infrastructure, people and trustworthiness of a firm, or fund, supported by independent verification.

It aims to answer questions for investors, such as:

- > "Do my assets exist?"
- > "Are they safeguarded from fraud?"
- > "Are they valued correctly?"
- > "Is this firm reliable?"

This, in turn, helps to avoid losses and the reputational damage of being associated with bad actors. Robust ODD helped investors and market participants avoid Madoff, FTX, Weaving, Theranos, Sam Israel, and Allen Stanford to name just a few.

Thankfully for the initiated, operational due diligence is well and truly understood as highly valued and important research. Without it, the words 'due diligence' are lost in a world of KYC/AML, background checks, cyber security, business continuity, outsourcing, compliance and regulation. All of these form PART of robust ODD, but do not constitute ODD.

ODD is a crucial tool and deserves its standalone, permanent, position high on the agenda

It is a key indicator of doing business transparently, safely and 'operational conviction', in the same way as investment professionals require 'investment conviction'.

ODD should not be a barrier, rather it can offer a means to grow, develop and thrive. ODD signals good features, providing a competitive advantage that plays a key role in the winning and retaining of clients. Done right, it is truly an enabler.

"With ODD as often the last hurdle to facilitate an investment, the requirements and attention sought from the IM in completing the ODD can strain the relationship. However, since the launch of perFORM we have seen a desire by IMs to prepare themselves effectively for ODD, to make the process as simple as possible for prospective allocators."

Historically, ODD has often been initiated by allocators who have already performed investment due diligence and approved an investment manager (IM). They then need to perform the ODD, possibly under time pressure and possibly with the assistance of investment consultants, who may be somewhat removed from the business.

With ODD as often the last hurdle to facilitate an investment, the requirements and attention sought from the IM in completing the ODD can strain the relationship. However, since the launch of perFORM we have seen a desire by IMs to prepare themselves effectively for ODD, to make the process as simple as possible for prospective allocators. We even launched a service to help facilitate this, our 'ODD Therapy' – to prepare IMs for institutional-grade ODD.

Risk management and client focused

We now offer a service where we perform our standard ODD review of an IM, but with them as our client, not the prospective allocator.

We don't award a 'pass' or 'fail'. Instead, we provide a high/medium/low risk assessment of the operational framework in order to enable the client to focus on the most important aspects for improvement; the client will only complete a factual accuracy check of the report before it is issued.

Where possible and additive, perFORM will complete an onsite visit. However, our review process is significantly less onerous and time-consuming than a data-heavy, sample-based controls-type audit. The ODD report process is relatively simple and quick to implement and maintain, and it is also cost-effective. Clients can benefit while continuing to focus on what matters most: growing business. We know they are busy.

The primary beneficiary of the report is the client, but consumers of efficient and high quality ODD research also benefit from the periodically updated and securely provided reports, free of charge.

For the client, the report is designed to help meet the ODD demands of allocators in a proactive, efficient and impactful way, significantly reducing the amount of time spent managing inbound due diligence requests and fast-tracking the operational due diligence process.

It should enable allocators to complete their work more efficiently and less onerously. Many are stretched with regard to resources and would benefit from practitioner-led solutions.

Finally, it is a very impactful demonstration of the client's institutional 'readiness' and willingness to reach, and remain at, operational best practice.

Does it replace all inbound ODD?

No - and nor should it, but it really does help make for a happier, healthier and longer, allocator/IM relationship.

More and more allocators are asking for our help with operational monitoring of their portfolios; how compelling it would be to say this is already covered and a research report is available instantly, without cost.

ODD is a highly visible demonstration of transparency. Upon request, we will announce completed reports (via our popular 'Due Diligence Matters' bulletin) and direct queries to the client who can provide a link to our report at their discretion. Consumers then access our ODD report(s), securely, via our IT portal. Further, clients get a perFORM logo to use on marketing materials, website etc.

Naturally, we all like ticking a box.

It is a selected purchase, a mark of success, an achievement, a "pass", an award, plus a way of expressing our likes, dislikes, personal characteristics and preferences. An ODD report is not just another tick in a box, it is a new approach to ODD.