What should a new fund manager think about?

Fund Structure

Audit/Tax Firm

Fund Administrator

Prime Broker

Information Technology

Staffing: In House vs. Outsourced

Method of Compensation

Trading Platform

Benefits

Office Space

Structure of the Management Company

Who is paying for research?

Fund Structure:

Does the fund manager anticipate receiving offshore or retirement account capital? If so a Master-Feeder structure typically makes the most sense. Otherwise at the onset a fund manager can open a Domestic LP and later convert to a Master-Feeder. A Master-Feeder will be more expensive than a Domestic LP, additional expenses include but are not limited to the following: additional audit fees, tax fees, directors fees, offshore legal counsel, Cayman Islands filing fees, among other expenses.

Audit/Tax Firm:

What is the fund manager looking for in an audit/tax firm? Do they want a name brand firm: ranging from a Big 4 to some of the larger mid-size firms or are they satisfied with one of the smaller firms in the industry. A smaller firm will be less expensive but may not have the same name brand recognition among investors.

Fund Administrator:

Similar to choosing an audit/tax firm, fund managers need to decide on whether to go with a large fund administrator, a mid-sized but still name brand administrator, or one of the smaller service providers in this space. In addition they must think about the type of services that they are looking for: NAV lite, month end NAV, or daily p&l as well as daily position and trade break reconciliation. In most cases, the larger the firm and the more services required the higher the fees will be, including the minimum fee charged by the firm.

Prime Broker:

Fund managers must choose an appropriate prime broker. Prime brokers can range from the large names (e.g. Goldman Sachs, Morgan Stanley, JPMorgan) to the smaller "Introducing Brokers" (e.g. BTIG, Jeffries, Concept Capital). The larger firms in this space will not always accept the smaller fund launches as clients and therefore it makes sense for the sub-$100mm fund launch to look at the introducing brokers. The introducing brokers often have relationships with some of the large prime brokers to providing clearing and custody services.

Information Technology:

Fund managers much choose between using a bare bones IT system, consisting of email (preferably a hosted Microsoft Exchange platform) and a cloud based file system (e.g. Dropbox). The bare bones system will enable a fund to get up and running, though will not meet with some institutional investors expectations for IT infrastructure. The other option is to go with an outsourced IT infrastructure which can either be a cloud based or an internal server system. Either of these options will be more expensive but will satisfy any institutional investors who may conduct due diligence on a fund. The cloud based solutions will typically be cheaper up front with a higher per month charge and the internal server will necessitate a larger upfront investment but will be less per month going forward.

Staffing:

Fund managers must make a number of decisions in staffing their new firm. In addition to investment staff, they need to think about the following:

An office assistant is often a good hire. They are typically not very expensive and can take care of a lot of the administrative tasks required when setting up the fund and the business. This will allow the fund manager to concentrate on more important items such as developing marketing materials, planning the portfolio, and raising capital.

In House vs. Outsourced:

CFO: The benefit of an outsourced CFO is that you are able to hire someone for a fraction of the cost of hiring a full-time in house CFO. While this role will at times require full-time hours, there are also downtimes when a fund manager may be better off not paying someone to sit in their office. Also, by working with an outsourced CFO the fund manager may be able to work with a CFO that has significantly more experience than if they hired an in-house CFO when faced with a limited budget. The downside is that you will not always have access to the CFO as they will be working with more than one client and will be offsite.

Trader: The benefit of using an outsourced trader is that you will only be paying a small service fee for the use of the trader. You also will have someone available 24 hours a day, as most outsourcing firms will have traders available 24 hours a day to cover all global markets. The negative is that, there is the possibility that the outsourced trader may not always work as hard for the fund manager in obtaining the best execution price for a trade, also the communication will not be as seamless as it would be if they were in the same office.

Method of Compensation:

A fund manager will need to determine whether or not, in addition to a base salary, they are going to pay their employees via a discretionary bonus, shadow points, or as partners of the firm.

Trading Platform:

A fund manager has two main choices for a trading platform. They may go with an execution only system such as Bloomberg's EMSX, REDI (Goldman), JETS (Jeffries), Neovest (JPMorgan), etc. or they may opt to use an OMS such as Eze Castle or Bloomberg's AIM. The decision will be based on the fund manager's needs and budget, with the OMS systems being more expensive and the execution only systems typically being free. Also, a fund manager may not require an OMS especially if they are not using multiple prime broker.

Benefits:

There are two main options to obtain benefits for the firm. A fund manager can either piece together a benefits package using multiple providers (payroll, health insurance, etc) or they can use a one stop shop Professional Employment Organization (PEO) for their benefits needs. The advantage to a PEO is that as a small firm they will be eligible for similar health insurance that typically only larger firms are eligible for. Also, all of their Human Resource needs would be consolidated and taken care of by the staff of the PEO. The disadvantages of the PEO are, while they offer a lot of benefits, they can be less flexible in terms of what is offered and you must follow their polices. Also, because of the administrative fees that can be slightly more expensive.

The fund manager will also have to decide what they want to offer their employees, e.g. how much to cover for health insurance, life insurance, retirement plan, etc. They also will want to ensure that they have the appropriate liability and other insurances for their business. Whether or not they choose to use a PEO, there are service providers that can discuss all of their options with them so that they can make an informed choice.

Office Space:

New fund managers may be hesitant to get themselves tied up in a long term lease and will want other options. The options include: sub-leasing a private office, renting space from an existing fund manager that has extra space, or leasing space in a shared executive suite. The decision will be based upon the fund managers needs and budget.

Structure of the Management Company:

The fund manager will need to choose either an LP or an LLC for the structure of the management company. There are positives and negatives to each structure. It is suggested that you consult with your attorney to determine which structure will best fit your business.

Who is paying for research?:

The fund manager will need to determine if either the fund or the management company will pay for research. Some people argue that the management fee charged by the fund should cover the research costs and others do not share this view. The fund manager will also need to determine, if the fund is paying for research, if they are going to charge the fund directly or use Soft Dollar to pay for research.