

Module 76.1 Quiz - Answers

Question 1

Compared with alternative investments, traditional investments tend to:

- A) be less liquid.
- B) have lower fees. ✓**
- C) require more specialized knowledge.

Explanation

Traditional investments typically have lower fees, require less specialized knowledge by investment managers, and are more liquid than alternative investments.

(Module 76.1, LOS 76.a)

Question 2

An investor who wants to gain exposure to alternative investments but does not have the in-house expertise to perform due diligence on individual deals is *most likely* to engage in:

- A) co-investing.
- B) fund investing. ✓**
- C) direct investing.

Explanation

With fund investing, due diligence on the fund's portfolio investments is a responsibility of the fund manager rather than the fund investors. Direct investing and co-investing require greater due diligence of individual deals on the part of the investor.

(Module 76.1, LOS 76.b)

Question 3

Management fees for a private capital fund are determined as a percentage of:

- A) invested capital.
- B) **committed capital.** ✓
- C) assets under management.

Explanation

For a private capital fund, management fees are a percentage of committed capital rather than invested capital. For a hedge fund, management fees are a percentage of assets under management.

(Module 76.1, LOS 76.c)

Question 4

For an investor in a private equity fund, the *least* advantageous of the following limited partnership terms is a(n):

- A) clawback provision.
- B) European-style waterfall provision.
- C) **American-style waterfall provision.** ✓

Explanation

An American-style waterfall structure has a deal-by-deal calculation of incentive fees to the GP. In this case, a successful deal where incentive fees are paid, followed by the sale of a holding that has losses in the same year, can result in incentive fees greater than those calculated using a European-style (whole-of-fund) waterfall. A clawback provision benefits the limited partners by allowing them to recover performance fees paid earlier if the fund realizes losses later. A clawback provision, coupled with an American-style waterfall, will result in the same overall performance fees as a European-style waterfall if the transactions occur in subsequent years.

(Module 76.1, LOS 76.c)