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CORPORATE counsel

IN THE NEWS

New Sheriffs in Town

by Tamara Loomis

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Like modern-day gold rush towns, hedge funds have sprung up all over the place, they've mined huge riches, and they've done business pretty much as they've pleased. But just as the law finally came to the Wild West, hedge funds will be placed under a regulatory yoke starting in February. In response, many funds are hiring general counsel and chief compliance officers for the first time. These new in-house lawyers face a situation that would be familiar to any frontier sheriff — establishing order in a place where the locals are used to doing what they want.

Claude Baum, the GC of Ore Hill Partners LLC, a New York-based hedge fund, says that fund managers “understand that they're cowboys in a way.” But, Baum adds, "They don't want to screw things up." Recent scandals at Millennium Partners, Canary Capital Partners, and Bayou Management have shown what happens when fund managers get too cocksure. A desire to avoid similar problems has contributed to the rising demand for in-house legal talent at funds.

"There was a big [hiring] push over the summer," says Andrea Stern, vice president of legal and compliance at Solomon-Page Group LLC, an executive search firm in New York. Stern says things have slowed down since, but "if a lawyer has a desire to go in-house [at a fund], now's the time to do it."

Hedge funds are investment vehicles favored by wealthy individuals and institutions (the minimum commitment typically ranges from $250,000 to $1 million) that engage in a range of aggressive strategies such as short-selling, arbitrage, derivatives, and program trading. The industry has exploded in recent years, to the point where more than 8,000 funds have a total of more than $1 trillion under management, according to Hedge Fund Research, Inc., a Chicago-based research group. This rampant growth has been partly fueled by the virtually unregulated status of hedge funds, which gives them more investment flexibility than regulated rivals such as mutual funds.

That all will change on February 1, when a new Securities and Exchange Commission rule takes effect. Any hedge fund with more than 15 investors and $25 million in assets must be registered with the agency by that date. Though about 5,000 funds aren't registered, the anticipated deluge of registrations has yet to happen. Many funds appear to be skirting the new rule by not accepting new investors, or by insisting that investors keep their money in the fund for two years or more. Either approach exempts a fund from registration.

Registration exposes hedge funds to a tangle of regulatory requirements: submitting financial disclosure reports, undergoing spot audits by SEC staff, and hiring a chief compliance officer. Although the SEC doesn't insist that the CCO be a lawyer (and even allows the job to be outsourced), most funds are filling the post with an in-house attorney, according to recruiters.

And though registration doesn't require a hedge fund to hire a GC either, many are doing so anyway — not just to help with regulatory compliance, but to advise the fund on increasingly complicated business transactions. While the first hedge funds stuck with simple stock trades, today's managers use a wide array of investment vehicles, up to and including leveraged buyouts.

When hedge funds make an in-house hire, they often tap midlevel and senior associates at their outside counsel, says Michael Lord, principal of Michael Lord & Company, a New York-based recruiting firm. He says that the ranks of midlevel associates at firms with big hedge fund practices have been "decimated" as a result. Lord adds that funds are enticing their new hires with starting compensation of $150,000–$300,000 for CCOs and $200,000–$1 million for GCs. The possibility of switching to the business side is also luring some lawyers to hedge fund jobs. Although it's relatively rare for in-house attorneys to get a piece of the equity, that still happens at smaller funds just getting established, says Lord.

Once they get there, lawyers often find that hedge funds are a far different place from "staid and stuffy" law firms, as Baum puts it. "Days are hectic and long, with different things coming at you from all sides," says Baum, formerly a partner at Brown Rudnick Berlack Israels. In April 2005 he became the first GC of Ore Hill, a fund with 20 employees and $1.4 billion under management. "You have to be a 'think on your feet' kind of person," Baum says.

Yasho Lahiri, who left Quantitative Financial Strategies Inc. in August 2005 after four-and-a-half years as the New York-based fund's GC and CCO, agrees. "The pace of being in-house at a hedge fund is a little like dog years," says Lahiri, now a partner in the New York office of Baker Botts. "Everything is a priority, and everything has to be done today. You somehow have to figure out how to get 48 hours of work done in a day." That's because many of the demands are extremely time-sensitive. Lahiri explains, "If a manager needs information for a transaction he's considering before the market opens, if he gets it any later than that, he might as well not get it at all."

Sylvie Durham seconds this job description. She spent three years as GC, CCO, and business development director at Abney & Holloway Management Resources, LLC, a small New York-based hedge fund with about ten employees. (In October 2005 she joined Greenberg Traurig as a partner.) "You have to be prepared for traders screaming at you on the phone, wanting an answer on a moment's notice, while somebody else is sitting in your office waiting for his answer," Durham says.

Especially at a small hedge fund, the GC doesn't have the benefit of wearing just one hat, Durham adds. "You need a very strong understanding of compliance, which a lot of lawyers don't have," she says. In addition, there's the "typical general counsel stuff" to deal with, like finder's fee agreements, lease negotiations, and employment matters, Durham says.

Though Durham and Lahiri left their hedge fund jobs to return to law firms, both say they enjoyed their in-house experience, and they count their former employers as clients, since hedge fund work is part of their practices. Durham says she left Abney & Holloway because she got "a very nice offer" from Greenberg Traurig. Lahiri says his hedge fund experience was "positive in every way," though the pace had started to get to him: "The last time I had a vacation was four years ago" — i.e., before joining QFS.

For now, lawyers like Lahiri and Durham are the exception to the rule. Stern, the executive recruiter, says that along with private equity funds, "hedge funds are the flavor of the year—everyone wants to go [to one]."

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