

HEDGE FUNDS: STRUCTURING, ADVISING, AND REGULATING
UC Berkeley School of Law, Boalt Hall
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Objectives:

The class introduces students to the legal landscape in which hedge funds operate. Students learn about the basic regulatory framework applicable to funds, structuring of funds, agreements among the parties involved with funds, and current trends. In addition the course will critically analyze the current regulation of funds and proposals for reform.

Prerequisites:

The class has no course prerequisites. Students who are interested in advising hedge funds, in regulating hedge funds, or in reforming the hedge fund industry will all benefit from the course. Students should have a basic understanding of the financial industry (at a New York Times level) and a general understanding of tax and corporate law terminology.

Course Format:

The majority of classes are lectures and class discussions covering, at a high level, key substantive legal and regulatory topics. The remaining classes are: 1) in-depth discussions of a current 'hot topic' and 2) guest speakers.

Course Grading:

The course grade will be determined by a written final examination. The examination will be open-book (class notes, assigned reading, and handouts only). Class participation will be considered in final grading if there are any final exam scores closely clustered around the P/H/HH thresholds.

Class Times and Office Hours:

Class will meet Wednesday evenings from 6:25pm to 8:15pm in Room 10. Office hours will be held each Wednesday in the law school café from 5:30pm until 10 minutes before class starts.

Lectures:

1. Hedge Fund Overview

- a) Distinctions and definitions of various pools of capital (venture capital, private equity, hedge funds, mutual funds, etc.)
- b) What is a hedge fund?
- c) History of the industry
- d) Important figures and funds in the industry (Robertson, LTCM, Soros, SAC, Renaissance, etc.)
- e) Strategies used by hedge funds (equity long-short, distressed, credit funds, etc.)
- f) Key terms used in the industry

Class Readings:

- 1) “An Introduction to Hedge Funds” by Gregory Connor and Mason Woo
<http://www.iam.uk.com/press/lse-publications/An-Introduction-to-Hedge-Funds.pdf>
- 2) Hedge Fund/Private Equity/Venture Capital matrix (distributed in class)

2. Hedge Fund Structuring: Regulation

- a) Investment Company Act of 1940 exemptions (3(c)(1) and 3 (c)(7) funds)
- b) Securities Act of 1933
- c) Incentive Fees
- d) Policy distinctions 33 Act/34 Act vs. 40 Act
- e) Investor profiles for various structures

Class Readings:

- 1) “Demystifying Hedge Funds: A Design Primer” by Henry Ordower
<http://blj.ucdavis.edu/archives/vol-7-no-2/Demystifying-Hedge-Funds.html>
- 2) The Laws that Govern the Securities Industry
<http://www.sec.gov/about/laws.shtml>

3. Hedge Fund Structuring: Tax

- a) tax overview and tax efficient structuring
- b) legal entity choices
- c) ‘Onshore funds’
- d) ‘Offshore funds’
- e) Master-Feeder structure/ Mini-Master Structure
- f) Investor profiles for various structures

Class Readings:

- 1) “Federal Income Tax Treatment of Hedge Funds, Their Investors, and Their Managers” By David Miller and Jean Bertrand
Pages: 309-323, 335-337, 377-385
<http://www.cadwalader.com/assets/article/081512MillerBertrandTaxLawyer.pdf>

4. Regulatory and Legal Framework (Funds)

- a) Board of Directors of funds (*Weaver*ing case in Cayman Islands)
- b) Fund launch (walk through all the aspects of a launch)
- c) CIMA/FSC registration and regulation
- d) 40 Act exemptions further discussion
- e) Private placement rules (Form D, 4(2), impact of JOBS Act, blue sky laws)
- f) Offering documents (disclosure requirements generally)
- g) Exchange Act Sections 13 & 16
- h) '34 Act (including impact of JOBS Act)

Class Readings:

- 1) *Weaver*ing Case (Grand Court of the Cayman Islands)
http://www.opalesque.com/files/20110826_Weavering_Judgement.PDF
- 2) Sample launch checklist and Offering Memorandum (distributed in class three)
- 3) Significant Changes to Rule for Private Securities Offerings
http://www.cov.com/files/Publication/03aebec8-81dd-4204-ba1a-3279509d041e/Presentation/PublicationAttachment/2797d54b-a54a-46fc-a36d-3f67c5f0b7e7/Significant_Changes_to_Rules_for_Private_Securities_Offerings.pdf
- 4) Section 13 SEC Reporting by Advisers and Brokers and Section 16 SEC Reporting by “Insiders” of Public Companies by Paul Hastings
<http://www.paulhastings.com/assets/publications/1827.pdf>
- 5) JOBS Act Quick Start: A Brief overview of the JOBS Act
Pgs. 5-15, 39-44, 61-65
<http://www.mofo.com/files/Uploads/Images/130200-JOBS-Act.pdf>

5 & 6. Regulatory Framework (Investment Advisors)

- a) Advisers Act of 1940
- b) Registration (analysis of SEC vs. State thresholds)
- c) Form ADV
- d) Fiduciary duties
- e) Fees, the custody rule, recording keep, code of ethics
- f) § 206 liability for failure to supervise (liability without scienter)
- g) Role of Chief Compliance Officer

Class Readings:

- 1) Investment Advisors Act of 1940 (as amended through P.L. 112-7, approved March 31, 2011)
<http://www.sec.gov/about/laws/iaa40.pdf>
- 2) Rules and Regulations, Investment Advisors Act of 1940 (Selected sections to be decided in class 4)
http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&tpl=/ecfrbrowse/Title17/17cfr275_main_02.tpl
- 3) Guide to SEC Investment Adviser Registration for Hedge Fund and Private Equity Fund Managers
http://www.bingham.com/Alerts/2011/02/~/_media/E87B98C6BC794D3FB2E1DD629DC5DE11.ashx
- 4) Planning a Hedge Fund Launch? SEC Registration Thresholds for Start-up Managers.
<http://www.rkollp.com/assets/attachments/Planning%20a%20Hedge%20Fund%20Launch.pdf>
- 5) Impact of the Dodd-Frank Act on Private Equity Funds, Hedge Funds and Their Investment Advisers
http://www.davispolk.com/files/Publication/66d6504a-7e38-43e2-b1f6-00e52e205c19/Presentation/PublicationAttachment/507520c9-230f-4669-a368-0622e2cbb2cf/091510_PE_NL.pdf

7. Investment Advisor Regulatory Compliance

- a) Personal account trading control
- b) Trade allocation policy
- c) Pricing committee
- d) Best execution and use of soft dollar (explanation of soft-dollars)
- e) Proxy voting
- f) AML

- g) ERISA ‘plan asset’ test
- h) Public filings (13F, 13D, 13G, 13H)
- i) Form ADV

Class Readings:

- 1) Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934
<http://www.sec.gov/rules/interp/2006/34-54165.pdf>
- 2) What to Do if Your Fund Becomes Subject to ERISA
http://www.morganlewis.com/pubs/IL_SubjectToERISA.pdf
- 3) Standard Pacific Capital, LLC’s ADV
http://www.adviserinfo.sec.gov/IAPD/Content/Search/iapd_Search.aspx

8. Fiduciary Duties

- a) History of Investment Adviser fiduciary duties
- b) Legal basis for an adviser’s duties
- c) Specific duties
- d) Standard of conduct

Class Readings:

- 1) “An Investment Adviser’s Fiduciary Duties” By Lorna Schnase
<http://www.40actlawyer.com/Articles/Link3-Adviser-Fiduciary-Duty-Paper.pdf>
- 2) S.E.C. v. Capital Gains Bureau (375 U.S. 180 (1963))
<http://www.sec.gov/divisions/investment/capitalgains1963.pdf>
- 3) S.E.C v. Steadman (967 F.2d 636 (1992))
<https://bulk.resource.org/courts.gov/c/F2/967/967.F2d.636.91-5130.91-5090.html>

9. Key Industry participants and the agreements governing their relationships

- a) Prime Brokers (asset protection issues)
- b) Derivatives counter parties (ISDA architecture)
- c) Custody Agreements
- d) Investment Advisor
- e) Auditors
- f) Trading counterparties
- g) Fund Administrators

Class Readings:

- 1) Trends in Prime Brokerage
<http://www.davispolk.com/files/Publication/030265d8-47e5-4de9-8a35-656619e6e4aa/Presentation/PublicationAttachment/6499d894-1466-4470-866f-6a4af93f322b/njordan.rcolby.practicallaw.article.apr10.pdf>
- 2) An Introduction to the Documentation of OTC Derivatives
http://www.isda.org/educat/pdf/documentation_of_derivatives.pdf
- 3) An Introduction to the Documentation of OTC Derivatives-“Ten Themes”
<http://www.isda.org/educat/pdf/ten-themes.pdf>
- 4) Lehman Brothers’ Bankruptcy -- Lessons learned for the survivors
<http://www.pwc.com/jg/en/events/Lessons-learned-for-the-survivors.pdf>

10. Investors/Marketing/Distribution

- a) Who invests in hedge funds?
- b) Side letters
- c) The due diligence process
- d) Private placement laws
- e) Sophisticated investor rules (and fee structures)
- f) HNW platforms and Third-party marketers
- g) Transparency
- h) Pay-to-play rules (CA-Lobbying rules)
- i) Prime Brokerage ‘Cap Intro’ services

Class Readings:

- 1) Principles and Best Practices for Hedge Fund Investors (Report of the Investors’ Committee to The President’s Working Group on Financial Markets)
http://www.amaicmte.org/Public/Investors_Committee_Report.pdf
- 2) The Spectrum of Hedge Fund Investors and a Roadmap to Effective Marketing
<https://www.wellsfargo.com/downloads/pdf/com/securities/hedge-fund-investors.pdf>
- 3) Improving the Relationship Between CalPERS and its Hedge Fund Partners
<http://www.calpers.ca.gov/eip-docs/investments/bus-opportunities/rmars/rmars-memo.pdf>

In-depth Modules:

11. The Short Selling Debates

- a) Mechanics of short selling
- b) Regulatory attempts to control abusive short selling
- c) Market efficiency and short selling
- d) Uptick rule
- e) Naked short selling (the company perspective)
- f) Form SH and international reporting requirements

Class Readings:

- 1) Background, overview and mechanics of a Short Sale
[http://en.wikipedia.org/wiki/Short_\(finance\)](http://en.wikipedia.org/wiki/Short_(finance))
- 2) Questioning the Benefit of Curbing Short Sales (NYTimes)
<http://www.nytimes.com/2011/12/16/business/questioning-the-evil-of-short-sales-high-low-finance.html?pagewanted=all>
- 3) Short Selling by Menachem Brenner and Marti Subrahmanyam
http://pages.stern.nyu.edu/~mbrenner/research/short_selling.pdf
- 4) Market Declines: Is Banning Short Selling the Solution? By Battalio, Mehran, and Schultz
http://www.newyorkfed.org/research/staff_reports/sr518.pdf

12. The Galleon Case: Understanding Insider Information issues for Hedge Funds

- a) Defining Material Non-Public Information
- b) History of regulation
- c) Different approaches to regulation
- d) Current and important cases
- e) Hedge Fund's use of Expert Networks

Class Readings

- 1) "The Law of Insider Trading" By Kaplan, Matteo, and Pfeffer
http://www.americanbar.org/content/dam/aba/administrative/litigation/materials/sac_2012/29-2_the_law_of_insider_trading.authcheckdam.pdf

- 2) Memorandum and Order, US v. Rajaratnam, S1 09 CR 1184, SD NY, August 16, 2011
<http://www.law.du.edu/documents/corporate-governance/criminal/rajaratnam/Memorandum-and-Order-US-v-Rajaratnam-S1-09-CR-1184-SD-NY-August-16-2011.pdf>
- 3) Government's Sentencing Memorandum, US v. Rajaratnam, S1 09 CR 1184, SD NY, August 9, 2011
<http://www.law.du.edu/documents/corporate-governance/criminal/rajaratnam/Governments-Sentencing-Memorandum-US-v-Rajaratnam-S1-09-CR-1184-SD-NY-August-9-2011.pdf>
- 4) Sentencing Memorandum on Behalf of Raj Rajaratnam, US v. Rajaratnam, S1 09 CR 1184, SD NY, August 9, 2011
<http://www.law.du.edu/documents/corporate-governance/criminal/rajaratnam/Sentencing-Memorandum-on-Behalf-of-Raj-Rajaratnam-US-v-Rajaratnam-S1-09-CR-1184-SD-NY-August-9-2011.pdf>

Expert lectures:

13. Raj Venkatesan and Doug Dillard, Co-Managing Partners, Standard Pacific Capital, LLC

Portfolio construction and process at a global equity long-short fund.

Class Readings:

[TBD]

14. Dave Lindberg, CFO, Standard Pacific Capital, LLC

Hedge fund accounting basics; FATCA

Class Readings:

[TBD]