HOW TO START A HEDGE FUND IN THE US 2016

LEGAL FRAMEWORK
Preparing and adjusting to legal changes

CAPITAL RAISING
Attracting sophisticated investors

TRANSPARENCY
Meeting the infrastructural requirements

Forward thinking is the first step

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The importance of possessing an all-encompassing knowledge of the hedge fund industry has always been of the upmost significance for managers, especially in the US.

A stream of new regulation and a steadily transforming legal framework have created a financial landscape which requires a thorough insight to progress in.

There is often the perception that starting a hedge fund in the US is an easy way to considerable wealth.

But an abundance of hidden risks are continuously overlooked in the early stages of a launch and can ultimately, and often do, lead to the downfall of the fund.

In the latest HFMcWeek’s How to start a hedge fund in the US 2016 report, we speak to market-leading figures including audit partners, fund administrators and global heads of international financial corporations.

These experts discuss the essential steps in how to launch a fund, and more importantly, how to help it prosper.

This report aims to provide a must-read guide for any individual within the industry, from emerging managers to the most established fund senior figures, HFMcWeek’s How to start a hedge fund in the US 2016 report offers unrivalled information in a notoriously ever-evolving marketplace.

Tom Simpson
Report editor
**LEGAL**

**WHAT YOU NEED TO KNOW ABOUT THE US HEDGE FUND INDUSTRY**
Ronald Honka, audit partner at Grassi & Co, examines why starting a hedge fund in the US isn’t as straightforward as first envisaged and highlights the hidden risks which are too often overlooked

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Jorge Hendrickson, head of sales and marketing at Opus Fund Services, provides a step-by-step guide to starting a hedge fund in the US

**FUND MANAGEMENT**

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**FUND SERVICES**

**BEHIND THE SUCCESS**
Christine Waldron, global head of US Bancorp Fund Services’ alternative investment solutions division, explores the importance of creative services in the US hedge fund sector

**FUND MANAGEMENT**

**SUCCESSFULLY LAUNCHING A PRIVATE INVESTMENT FUND**
Ron Gelfn and Daniel Viola, of Sadis & Goldberg, speak to HFMWeek about how to effectively structure a private investment fund

**FUND SERVICES**

**HEDGE START-UP ESSENTIALS**
Andrew Dougherty, North American head of alternative and institutional solutions for BNP Paribas, discusses the major changes that the hedge fund industry has seen over the past decade and advises on the essential points to consider when starting a hedge fund in the US

**FUND SERVICES**

**HELP YOUR HEDGE FUND FLOURISH**
Anchin, Block & Anchin LLP’s Jeffrey Rosenthal, CPA, CGMA and partner-in-charge of financial services practice, speaks to HFMWeek about the developing challenges facing emerging hedge fund managers

**FUND MANAGEMENT**

**HEDGE FUND FIRST STEPS**
Joseph Cassano, audit senior manager at WithumSmith+Brown, discusses the initial steps and key considerations of starting a hedge fund

**FUND SERVICES**

**SOLUTIONS FOR AND BEYOND THE START-UP STAGE**
Palak Patel, global head of product development for Bloomberg’s Asset and Investment Manager (AIM), talks to HFMWeek about how choosing the right service providers can help fund managers meet challenges through different stages of their fund’s growth
New hedge funds face some of their toughest challenges as they ramp up strategy, execution and technology all at the same time. Bloomberg Asset and Investment Manager (AIM) offers a complete order and execution management system (OEMS) designed to help startup funds launch quickly and seamlessly.

Combining professional-grade technology with a fully managed and hosted infrastructure, and backed by a global service and support team, AIM allows new funds to simplify investment operations, reduce operational risk and minimize both upfront infrastructure costs and long-term overhead. A solid foundation for today. Scalability and flexibility for tomorrow. AIM gives you the best of both.

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WHAT YOU NEED TO KNOW ABOUT THE US HEDGE FUND INDUSTRY

RONALD HONKA, AUDIT PARTNER AT GRASSI & CO, EXAMINES WHY STARTING A HEDGE FUND IN THE US ISN’T AS STRAIGHTFORWARD AS FIRST ENVISAGED AND HIGHLIGHTS THE HIDDEN RISKS WHICH ARE TOO OFTEN OVERLOOKED

Starting a hedge fund in the United States may sound like an easy way to substantial wealth, but the process will prove to be challenging. The emerging manager must have an entrepreneurial mindset and think like a business owner, not solely as a portfolio manager. Initially, a significant amount of time will be spent managing overhead, human resources and marketing (capital raising); as well as IT and network infrastructure. Federal and state securities laws will present additional challenges to an emerging manager not prepared for the regulatory process. Managers must be aware that hedge funds and their advisors are governed by the Securities Act of 1933 (the Securities Act), the Securities Exchange Act of 1934 (the Exchange Act), the Investment Advisers Act of 1940 and the Investment Company Act of 1940 (the Investment Company Act).

CAPITAL RAISING
Raising capital is highly competitive and managers looking to attract sophisticated investors must be able to prove that their strategy has historically been successful under differing market conditions and require the emerging manager has an appropriate mix of experience and business savvy. Family and friends typically tend to be the first choice for capital for emerging managers and, due to their relationship with the manager, may not require an extensive proven track record. Once a track record is established (spanning multiple years) capital raising activities begin to focus on fund-of-funds, family offices and high-net-worth individuals. Introductions to these investors can be facilitated through capital introduction groups. Managers may also obtain early stage capital from seed investors, who may provide support services, in exchange for a share of management and performance fees and possibly an ownership stake in both the management company and general partner entity. Ultimately, managers will want to attract institutional investors. Managers interested in obtaining institutional assets must, in the early stages of the fund’s existence, develop the necessary infrastructure. Healthy returns, without the proper infrastructure, will not be sufficient to win institutional investors. Characteristics of a proper infrastructure include; vigorous compliance function, well-established management team, transparency, excellent service providers and a thorough risk management programme.

MANAGER COMPENSATION
Due to the competitive nature of capital raising, the traditional 2% and 20% compensation model for managers has been subject to intense scrutiny, managers must be willing to negotiate management and performance fee arrangements for long-term capital commitments. It’s not unusual for managers to accept significantly lower management fees, include performance hurdles and adopt lifetime performance fee arrangements.

INVESTOR BASE AND FUND STRUCTURE
Identifying the investor base will help in determining the fund structure. Private funds, including hedge funds and private equity funds, are excluded from the definition of an investment company and, as such, are not registered under the Investment Company Act. The majority of start-up hedge funds in the US are structured under Section 3(c)(1) of the Investment Company Act, which limits the beneficial ownership to not more than 100 accredited investors. Section 3(c)(1) funds must comply with Rule 506 of Regulation D which is considered a safe harbour for the private offering exemption of Section 4(2) of the Securities Act. Section 3(c)(1) funds are typically domiciled in the US as the initial investors for emerging managers tends to be friends and family. Other funds may be structured under Section 3(c)(7) of the Investment Company Act which must be owned by qualified purchasers. Section 3(c)(7) funds are primarily used by funds with institutional investors.

SERVICE PROVIDERS
The emerging manager must choose a mix of trusted service providers to help them achieve their goals.
**Attorneys** – assist in the creation of the formation documents (documents filed with the government establishing the entities’ existence); operating documents of the management company and general partner (the governing documents providing for the rights of the founders); investment management agreement (the agreement between the fund and the management company defining the services the management company will provide to the fund and the fee the fund will be paid for those services); fund offering documents or private placement memorandum (provides an overview of management, strategy, fees and risks); limited partnership agreement (outlines the terms of the fund and the rights of an investor, this is the legal governing document of the fund) and; subscription agreement (describes the steps necessary to invest in the fund, specifies the subscription amounts and outlines the terms in which the investment is being made).

**Administrator** – serves as the official record-keeper, provides back office accounting such as; trade reconciliations, investor allocations, reporting of net asset values, and maintains the general and subsidiary ledgers. The administrator will also: process investor subscriptions, redemptions, transfers and assignments; maintain investor registers; and prepare monthly investor communications and statements. On an annual basis, the administrator is instrumental in the annual audit and tax reporting as they prepare financial statements and supporting schedules for both the fund auditor and tax preparer.

**Prime broker** – provides trading and custodial services to the fund and may provide leverage. Funds of a smaller size may choose to use an introducing broker, who has partnered with a prime broker, as their fee structures are tailored more towards smaller funds.

**Auditor** – performs a crucial role in assisting investors to make informed decisions. Through the independent work performed by the auditor, investors place reliance on the annual financial statements and in some instances, separately reported performance data. Institutional investors will require performance data and annual financial statements be audited by an audit firm recognised for its proficiency in the hedge fund industry.

**Tax Advisor** – ensures that investor needs are met through advantageous tax structures, timely and accurate reporting of K-1s to investors, and helps the manager comply with tax-related issues.

**Compliance** – A robust compliance function assists the fund manager to traverse the regulatory environment, implement a risk management framework and meet the requirements of regulatory agencies (SEC, CFTC, etc.).

**TRANSPARENCY**
Perhaps the most significant key to success for emerging managers is transparency. Investors will no longer accept great returns with limited information. Investors want to know not only what is in the fund, but also what the fund’s risk characteristics are. Providing greater transparency requires the infrastructure to report more data which can become burdensome to new managers as investors tend to place more value on the components of transparency; regulatory reporting, infrastructure, operations and service providers, than managers. Choosing the correct mix of trusted service providers will help increase the fund’s level of transparency, and, the higher the level of transparency provided, the higher the level of credibility – which in turn equates to a higher level of success. 

**MANAGERS INTERESTED IN OBTAINING INSTITUTIONAL ASSETS MUST, IN THE EARLY STAGES OF THE FUND’S EXISTENCE, DEVELOP THE NECESSARY INFRASTRUCTURE**
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ESSENTIAL HEDGE FUND GUIDANCE

Jorge Hendrickson, Head of Sales and Marketing at Opus Fund Services, provides a step-by-step guide to starting a hedge fund in the US.

Opus Fund Services is a leading global fund administrator with tremendous expertise in the new launch market. We provide clients with extensive support during the launch process and we are passionate about working closely with entrepreneurs. Below is a guide for navigating the process. Please use our guide as a resource.

The team – A strong team of individuals with complementary backgrounds who can collectively run all aspects of the fund businesses (investment and non-investment) is the key to success. Investors want to know that all bases are covered and that every individual is properly equipped in handling their responsibilities. If the launch budget does not support hiring a full team on day one, there may be other ways to build a well-rounded team.

First of all, find an entrepreneurial partner to join the firm in the early days. Since the fund cannot afford to compensate with market salaries, this partner would be offered equity in the business. A well-rounded COO who has the ability to run the business and handle all non-investment related activities may be a great addition.

Secondly, outsource CFO, COO, CCO and trading roles. The outsourcing of these functions is an acceptable business strategy. The fund can consider hiring these roles internally when the budget allows for it.

FUND STRUCTURE

Managers should work closely with their legal counsel to determine what fund structure makes sense. Much of this will be driven by the investor base. Common fund structures include:

- **Domestic standalone** – Typically a Delaware LP, this fund allows for investors who are US residents
- **Offshore standalone** – For non-US and US tax-exempt investors. Cayman and BVI are the most common domiciles
- **Mini-master** – Two-entity structure. Typically an onshore master fund and offshore feeder
- **Master-feeder** – Three-entity structure. Two feeder funds (onshore and offshore) investing directly into the master fund. All investments are made at the master fund level. Investors subscribe into the appropriate feeder fund
- **Parallel or side-by-side** – Two standalone funds (onshore and offshore). Each fund operates independently and makes their own direct investments

OTHER STRUCTURAL OPTIONS AND TRENDS

**Series** – At Opus, we are seeing a trend among managers launching Series, in order to provide investors with the ability to customise exposure to certain parts of the overall fund’s portfolio. For example, a FOF may offer Series A where investor exposure is limited to the fund’s investments into underlying funds ABC and XYZ, but would not be exposed to any other portfolio holdings. Each Series has its own set of investors, investments, fee classes and expenses.

**Special Purpose Vehicle (SPV)** – A standalone entity that is launched specifically for one investment, security or series of investments. Multiple investors may invest.

**Fund of one** – A standalone fund that is launched specifically for one investor. Unlike a Separately Managed Account (SMA), the manager retains control of the assets and maintains any custody relationships.
**FUND TERMS**

Fund documents will outline all fund terms. There is much discussion about what terms are reasonable, marketable and acceptable to the investor community and structuring terms correctly is of utmost importance. Examples of fund terms:

- **Minimum investment** is the minimum subscription that will be accepted into the fund. The General Partner (GP) has the discretion to allow investments below the minimum.
- **Subscription/redemption frequency and notice period** – these terms should line up with the investment strategy. For a liquid strategy (for example, L/S Equity), monthly subscriptions and redemptions may make sense operationally. Quarterly redemptions with a 30-day or 60-day notice is most common. For a fund running an illiquid investment strategy, an investor may be more open to stricter redemption frequencies.
- **Lockups** exist in order to establish a commitment period and to restrict investors on when they can redeem their investment. A one-year lockup is most common but may be longer depending on the investment strategy. Soft lockups allow for redemption but carry a penalty (for example, 3% penalty on the redeemed amount).
- **Management and incentive fees** – While 2/20 are still common fees, both have come under scrutiny over recent years as hedge fund performance has struggled. For example, management fees have come down closer to 1.5%. Management fees are typically paid monthly or quarterly (in arrears or in advance) and incentive fees are crystallised annually (accrued monthly). The management fee is paid to the investment manager (IM) and the incentive fee to the GP. Management fees are typically used to pay operating expenses (salaries, rent). Incentive fees are typically re-invested into the fund. Fund fees should keep the investment strategy and investor base in mind.
- **High Water Mark (HWM)** – Established to restrict the manager from being paid an incentive fee unless performance surpasses the previous account high.
- **Hurdles** – Incentive fees are paid if performance surpasses a pre-established hurdle or metric, such as a fixed return (5%) or index (S&P500).

**Capital calls, distributions, additional closings** – Private equity managers need to establish and outline the fund workflow and whether there will be capital calls, distributions or additional closings.

**SELECT CORE SERVICE PROVIDERS**

- **Fund administration** – The fund administrator serves as the fund’s books/records, strikes the NAVs and reports to the fund and investors. NAV frequency is typically monthly basis for hedge funds and quarterly for PE/VC funds. Fund administrators also provide investor services (on-boarding, AML/KYC), banking services (fund account opening, cash reconciliations, wire processing), draft GAAP Financials and audit/tax support.
- **Legal** – Fund and management company entity formations. Legal drafts all fund and management company documents. If there is a seeder, the operating agreement will reflect accordingly.
- **Audit/tax** – Year-end audit and tax prep, including K-1s. These firms can also provide managers with estate planning and with attestation services – performance verification of historical investment activity.

**Prime brokerage/custody** – Clearing and custody of cash and securities, margin financing, securities lending, trading technology and reporting. Services vary depending on the portfolio and fund needs. Custodians also provide custody/financing services to PE, VC, FOF, Lending and physical asset funds.

**SELECT OTHER PROVIDERS**

The manager should also focus on selecting other service providers:

- **Fund banking** – The account opening process for the fund can be driven by the fund administrator. Each fund (master and feeders) will have a bank account that is used for investor activity (subscriptions, redemptions) and for paying fund expenses and management fees
- **Management company banking** – Bank accounts used for non-fund expenses (for example, rent, salaries, IT) and to receive management fees
- **Compliance consultant** – Compliance manuals, SEC registration, regulatory filings
- **IT managed services** – Network, hosting, telecommunication, disaster recovery, business continuity
- **Order management system** (OMS)
- **Portfolio management system** (PMS)
- **Risk reporting**
- **Insurance** – E&O, BOP, D&O, liability, cybersecurity, key man, etc.
- **Professional Employer Organisation** (PEO)
- **Office space** – Shared office suite, sub-let, management company rental
- **Marketing collateral** – pitch book, tear sheet, website, due diligence questionnaire (DDQ)
- **Third-party marketing**
- **Staffing/recruiting**

**MARKETING COLLATERAL AND ASSET RAISING**

Managers should develop marketing collateral that clearly introduces the fund, its team, strategy, portfolio, risk management process, terms, infrastructure and service providers. Collateral includes the pitch book, tear sheet, a logo, a website and a DDQ. Managers need to identify, draw up and then execute a sales and marketing plan in order to raise assets in a strategic and methodical way. Appropriate resources and budget should be allocated to sales and marketing.

While the above outline includes details at a high level, individual funds may require very unique and varying levels of support. Each hedge fund launch has its own set of specific circumstances and timing may vary greatly. Leveraging your partners, industry peers and service providers during the process will help tremendously avoid delaying or timely and costly mistakes. Launching a fund is an exciting time and a huge step into entrepreneurship! At Opus, we are here to help.
Withum — Charging the way through the ups and downs of the financial market.

BE IN A POSITION OF STRENGTH™
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o, you want to be a hedge fund manager? After several successful years as a trader or analyst with a money manager or wire house, you want to venture out on your own to start a hedge fund, so where do you begin?

Well, starting a hedge fund requires focus, skill, and patience in hiring your own staff as well as the appropriate service providers to support your investment strategy. Those service providers include a law firm that specialises in fund formation as well as ongoing regulatory support. Next, select a prime broker that will provide you with trading technology, global execution and custodian services, reporting, operational support, capital introduction, soft dollars, and an affordable fee structure. And lastly, you will need to engage a fund administrator to manage investor subscriptions to your fund, provide supplemental reporting, and calculate the monthly NAV of the fund. The auditing firm is usually the last service provider to be hired by an emerging manager, and typically will be done toward the latter months of year one in operation.

LEGAL
After completing your research on legal representation, you make your decision to engage a law firm. For most emerging managers, the first meeting is a consultation to begin the process of preparing your offering and corporate documents. As an emerging manager, you should be well-prepared to answer questions pertaining to your fund’s structure, (single fund or master feeder, onshore versus offshore, type of strategy and traded products, fee structure, bios of key personnel and so on). This process can take approximately four weeks due to revisions in the offering documents, as well as the submission of corporate filings. The initial start-up costs for fund formation documents can be substantial, but in the long-run, it is money well spent since these are the primary documents that are presented to your potential investors and service providers.

Prime Broker
Selecting the appropriate prime broker is a very important consideration that an emerging hedge fund manager must undertake. It is imperative that you conduct your due diligence to make certain that your prime broker’s offered products, services, infrastructure, and support will benefit your strategy and will enable you have all of the necessary services you require to be successful. As an emerging manager, your focus needs to be on generating alpha and raising assets, not getting involved in time consuming operational issues. Remember, you are an emerging manager and keeping costs to a minimum during the early stages of your fund is imperative.

In evaluating a prime broker, it is very important for you to understand the requirements, cost structure, capability, and ongoing support. Are there any monthly minimums or AuM requirements imposed, if so, what are those requirements? Next, there should be a discussion on the product offering and if applicable, the international capability of your prime. Some prime brokers do not support every asset class, and if your strategy does not fit the product offering, you need to continue your search for another prime.

Since trading capabilities are an important consideration, you will need to address this topic in greater detail. Discuss your preference and available options that you may consider, for example electronic trading, order desk, or being covered by an institutional sales trader. Understanding your prime broker’s commission structure for self-directed trades, as well as ‘away trades’, and miscellaneous fees should all be documented and disclosed. A thorough review of your prime’s offered trading platforms, reporting capability, margin and risk requirements, and ongoing support should be reviewed with your prime broker before committing to a relationship.

Some prime brokers offer their hedge fund clients a capital introduction programme. Some emerging managers may be successful in getting capital and others...
may not be so fortunate. Keep in mind that building a good performance track record during your first year is critical for obtaining investor capital and that should be your focus. In the meantime, seeking capital from family and friends initially is always a good strategy in the early stages of your fund.

FUND ADMINISTRATION
The role of the fund administrator is to assist the emerging manager in serving their investors and to act as an outsourced department to handle monthly net-asset value and performance fee calculations. In evaluating a fund administrator, you should consider their technical skill, responsiveness, reporting capability and experience in dealing with your specific investment strategy. When interviewing an administrator, it's important to understand their requirements and capabilities as it relates to your strategy. Are there monthly minimums for engaging their services; if so, do these minimums increase when your AuM increases? What type of reports are available and their overall capability? These are all questions that you should ask so that you can better manage your cost structure and services during the early stages of your fund.

ACCOUNTANTS
Accountants and auditors play an important role in providing your fund with audit services and preparation of K-1s for the fund’s partners. The auditor performs the most important function of reviewing your financial statements and the capital accounts of your investors. Their review will be focused on making certain that accurate accounting controls, operational and trading procedures have been followed.

ADDITIONAL SERVICE PROVIDERS
For most emerging managers, the core team of lawyers, the prime broker, fund administrator and auditor are sufficient for a start-up hedge fund. Many of the infrastructure services that are required by an emerging fund are provided by the prime broker and custodian. However, at some point, your fund will be required to incorporate many services on their own as the fund’s assets and investor base grow. Those services may include further developing your fund’s technology infrastructure, trading capability, expanding the office space, liability insurance, medical and retirement plans, and the list goes on and on.

There is no shortage of firms that can assist a hedge fund in implementing a plan for expansion, but for the moment, as an emerging manager starting a new hedge fund you should concentrate on three specific goals:
1. Selecting experienced staff and the very best service providers
2. Building a good track record of solid performance
3. Practise, practise, and practise your pitch in soliciting new investors for your hedge fund.

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Christine Waldron, Global Head of US Bancorp Fund Services’ Alternative Investment Solutions Division, Explores the Importance of Creative Services in the US Hedge Fund Sector

HFMWeek (HFM): In terms of US Bancorp Fund Services’ (USBFS) new client portal, Pivot, how successful has it been since launching in late 2015 and are there any changes to be made?

Christine Waldron (CW): Since the soft release in late 2015, the portal has been very successful. We unveiled it to a range of new clients as well as our existing clients, who partnered with us on the design. Because of the immediate success, there are no imminent alterations to be made, although we do have long-term plans for regular releases of new functionality. To date, clients have thoroughly enjoyed the ability to manoeuvre across the entirety of our security services offering in a single solution. That versatility has been massively beneficial to clients, particularly those who frequently use our custody and fund administration services.

Our plans are to have quarterly releases for the foreseeable future to introduce new functionality and innovative features. We want to make sure the portal stays fresh, since too often portal technology is launched and then does not get regularly enhanced to meet changes in industry needs and client expectations. When ongoing improvements are not applied, it often results in a massive rebuild of the technology. This can be incredibly disruptive to clients as well as your overall market position. We want to make sure our portal avoids issues such as these by keeping the design and functionality fresh.

HFM: Apart from Pivot, what other innovative services do you provide to respond to clients’ needs?

CW: The needs surrounding data management and reconciliation with our clients is huge. In terms of meeting client’s needs, we have harnessed our technology by allowing our clients to interface with our environment in multiple ways. Alongside our portal is an application clients can access. The application is very valuable since it allows them to augment, query and extract data in our data warehouse to meet their needs. Instead of the clients receiving all of our data and maintaining it within their data warehouse, clients can actually add data fields to our data warehouse to better support their reporting needs and eliminate the cost of maintaining and storing all of this data internally. Our portal, application and file delivery solutions all use the same single data warehouse, allowing for consistent reporting and data consumption by whatever user interface a client may want to use. Between the portal, which allows on-the-go access, and the application, that ultimately supports their data service needs, our technology solutions complement one another and that’s the differentiator for us.

HFM: USBFS will offer an enhanced middle office offering in 2016, how will this affect the trade processing, risk, collateral and performance capabilities?

CW: It enhances them. Our offering is going to become more robust; we’re going to start to be able to provide clients
with greater transparency into the processes as well as services we previously have not supported, such as collateral optimisation. We plan to partner closely with our clients to ensure our offering is aligned with their service needs.

**HFM:** What substantial upgrades to technology systems and infrastructure can we expect to see in the next 12 months at USBFS and Quintillion?

**CW:** We have upgrade plans for our core infrastructure. Last year, Quintillion migrated into the bank’s data centre, which provided an opportunity to re-size the environment for future growth with all new hardware. This also allowed us to apply more robust cyber-security and overall security management into the platform. That was a large investment that we made in 2015. Both USBFS and Quintillion will focus on upgrading all our core engines to more current versions in 2016. It is common for people to not take upgrades as regularly as they should and we really strive to make sure we are on the latest versions of all of our core operating engines.

**HFM:** How does USBFS intend to expand the regulatory services team in the US and in Europe, and how will this support your clients’ regulatory filings?

**CW:** This is our primary focus in 2016. Our regulatory service team is being expanded, and we’ve already made some key strategic hires both in Europe, through Quintillion, as well as in the US. Our hires are being led by our regulatory team, which is headed up by Kent Barnes, who is an experienced attorney and an industry leader. Our service is going to be more than simply providing data to third parties to help prepare the offering. It will be expanded to allow us to manage clients’ regulatory filings and exams from start to finish. It will be comparable to how we support our US regulatory filings for our US mutual fund clients.

**HFM:** What industry trends do you expect will be of the most significance to HFAs in the next 12 to 18 months?

**CW:** We will be certainly monitoring regulatory changes, as the future direction of these changes will be absolutely critical. I think the hedge fund industry is under a lot of scrutiny in terms of performance and return and as a result of this, we will start to see greater transparency into how funds are performing against their stated objectives. While greater transparency has been a focus for years and progress has been made, what you haven’t necessarily seen is how the holdings and the performance stack up against what the stated objectives were as laid out in the governing documents and marketing materials. Correlation and comparison, that’s the next step we will need to be taking in terms of transparency reporting.
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Successfully launching a private investment fund, involving hedging strategies, private equity, venture capital or real estate, depends upon selecting the proper corporate structure and complying with regulations promulgated by regulatory agencies. These agencies govern funds and their managers in the US, including the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC). Under certain circumstances, managers based in the US may also be subject to oversight by non-US based regulators.

Structuring a fund involves both the creation of one or more entities through which investments will be made (domestic and offshore funds), as well as the creation of one or more management entities through which services will be provided to the funds (the general partner and/or the investment manager). The structure and domicile of the fund is primarily dependent upon two variables:

- The nature and demographics of the prospective investors
- The investment strategy employed by the manager

The structure and domicile of the manager is primarily determined by the citizenship and tax considerations of its principals, as well as the regulatory regime of the domicile.

**ECONOMIC ANALYSIS**

In determining whether to form both a domestic and an offshore fund, it is advisable to determine the amount of anticipated assets which will be invested in the funds within a few months after the launch of the funds. In short, the anticipated aggregate investment at, or shortly after, the launch of the business may not justify the formation of both a domestic fund and an offshore fund. To create both may impair the manager’s ability to survive due to the organisational expenses and the costs of maintaining both domestic and offshore funds. With early stage managers, cash burn is often overlooked and can be critical to the survival of the newly formed manager. The manager’s success depends upon having the opportunity to establish a proven track record.

**SIDE-BY-SIDE, MASTER-FEEDER & MINI-MASTER STRUCTURES**

Managers seeking to launch both domestic and offshore funds have several options available in structuring. The three most common structures are side by side, master-feeder and mini-master.

In a side-by-side structure, the domestic fund and the offshore fund make direct investments pursuant to the investment strategy and trade tickets are allocated between the domestic fund and the offshore fund.

In a master-feeder structure, a third entity is created (master fund) and the domestic fund and the offshore fund, rather than making direct investments, invest all of their assets into the master fund and in turn, the master fund makes the investments on behalf of the domestic fund and the offshore fund.

In a master-feeder structure, a third entity is created (master fund) and the domestic fund and the offshore fund, rather than making direct investments, invest all of their assets into the master fund and in turn, the master fund makes the investments on behalf of the domestic fund and the offshore fund (often referred to as the domestic feeder and offshore feeder).

The mini-master structure generally is comprised of two entities: an offshore feeder and a master entity. While the offshore feeder is taxed as a corporation to benefit US tax exempt investors and block UBTI, the master entity may be structured for tax purposes as a partnership. Rather than the US-based manager receiving its incentive as a fee
from the offshore fund and being subject to ordinary income tax, the US-based manager may receive the incentive as an allocation from the master entity, in an attempt to benefit from capital gains tax treatment.

There are many legal and commercial drivers in determining the ideal structure. For example, if the strategy calls for significant investment in illiquid or thinly traded positions which are difficult to allocate among two brokerage accounts, a master-feeder structure may be preferred as the investments will be allocated on a pro rata basis at the master fund, yet only require the manager to purchase and sell the positions through one brokerage account.

Also, in many transactions involving early stage or ‘seed’ investment, if the seeder is located offshore, it may prefer a master-feeder structure so that all fees and allocations may be taken at the master fund and thus avoid the US tax regime. Conversely, employing a tax efficient strategy for US taxable investors may be of little benefit or detrimental to US tax-exempt investors and non-US nationals. Thus, a side-by-side structure allows the manager the ability to employ tax efficiency with the domestic fund, while maximising the entry and exit points of securities positions without regard to long term tax gains for the offshore fund.

**STRUCTURING & DOMICILE OF THE MANAGER**

The structure and domicile of the manager is primarily determined by the citizenship and tax considerations of its principals. The majority of funds managed by US domiciled entities are structured as either limited liability companies or limited partnerships, which are taxed as flow-through vehicles (rather than as corporations).

In circumstances involving non-US persons, and if they own the majority of equity in or receive the majority of the economics from the manager and their interests are controlling, the manager may be organized in an offshore jurisdiction to accommodate the tax needs of the non-US persons.

**REGULATORY ANALYSIS FOR THE MANAGER**

Managers must also evaluate the various exemptions associated with adviser registration with the SEC and/or the CFTC, depending on the fund’s investment strategy. For example, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) introduced new registration requirements based on the total amount of assets managed in the US instead of the number of clients advised by the manager.

As such, a manager that only manages funds in the US will be required to register with the SEC, appoint a chief compliance officer and implement written compliance procedures subject to review from the SEC, if its ‘regulatory assets under management’, which includes the assets managed and any leverage utilised by the manager, exceeds $150m. Non-US based managers may also be required to register with the SEC and/or the CFTC if they cannot rely on exemptions from registration.

Likewise, managers are required to verify the tax status of the investors in a fund under the Foreign Account Tax Compliance Act, OECD Common Reporting Standards and to comply with the relevant blue-sky requirements for offers made to investors residing in the US.

**CONCLUSION**

It is important to use law firms with corporate, tax and regulatory experience in connection with structuring and maintaining hedge funds. Failure to properly structure your firm will have material opportunity costs.

**SOME RECENT REGULATORY DEVELOPMENTS**

**Accredited Investor Standard:** Under the Dodd-Frank Act, the SEC is required to review the ‘accredited investor’ definition every four years and revise this standard if necessary. In December 2015, the SEC issued a report proposing, among other changes, increasing the income threshold from $200,000 to $500,000 and the net worth threshold from $1m to $2.5m. Any revisions to the definition of an ‘accredited investor’ will likely require amendments to a fund’s offering documents.

**Form ADV Amendments:** Proposed Form ADV amendments would require managers who are registered as investment advisers with the SEC to provide additional information to the SEC and investors, including aggregate information related to assets held and the use of borrowings and derivatives in separately managed accounts. Additional information would also be required regarding an adviser’s business, including branch office operations and the use of social media. The SEC expects to release the revised Form ADV during 2016.

**Cybersecurity:** The SEC’s Office of Compliance Inspections and Examinations examined 49 registered investment advisers and 57 registered broker dealers in 2014 and in January 2015 reported that 74% of the registrants interviewed experienced a cyber-related incident. In September 2015, the SEC brought their first enforcement case against an investment adviser for allowing a breach of data to occur, exposing personal identifiable information of the adviser’s clients to an unknown hacker. Moreover, advisers registered with the CFTC are required to have written policies and procedures regarding cybersecurity controls and incident reporting by 1 March 2016.
HEDGE FUND START-UP ESSENTIALS

ANDREW DOUGHERTY, NORTH AMERICAN HEAD OF ALTERNATIVE AND INSTITUTIONAL SOLUTIONS FOR BNP PARIBAS, DISCUSSES THE MAJOR CHANGES THAT THE HEDGE FUND INDUSTRY HAS SEEN OVER THE PAST DECADE AND ADVISES ON THE ESSENTIAL POINTS TO CONSIDER WHEN STARTING A HEDGE FUND IN THE US

HFMWeek (HFM): What are the major trends impacting your hedge fund clients right now?
Andrew Dougherty (AD): We’ve seen a shift in hedge funds’ ability to secure the level of financing and access to credit that they have historically enjoyed. In recent years, many of the world’s largest investment banks conducted balance sheet optimisation exercises in order to meet more stringent regulatory requirements. Although financing temporarily loosened, we are seeing access to credit once again tightening and a new cycle emerging whereby hedge funds are seeking additional prime brokerage and financing counterparties.

HFM: When launching a fund, what are the major considerations the founders should consider?
AD: It has become increasingly important to have a long-term distribution strategy. A fund needs to consider what investors it will market to, as well as the geography and classification of those investors. As a start-up, the significant questions to ask are: “Will we primarily target high-net-worth individuals, family offices or institutional investors, and will we focus on the domestic US market or will we also target Europe, Asia and Latin America?” The answers become the determining factor for the structure of the fund itself – whether a fund is set up as a single entity domiciled within the US, or as a side-by-side fund with an offshore component (a master feeder structure or mini-master, for example). Major overseas regulations need to be considered. If there is an ambition to distribute globally, especially in Europe, regulations such as the AIFMD come into play. This directive carries significant requirements in terms of transparency, reporting, liquidity, depositary banking and custody. Those requirements will set the stage for the types of relationships and service providers that fund managers will require prior to launch. Getting the structure right from the start is critical.

From an operational perspective, two important factors to consider are the optimisation of the front-to-back operational structure of the fund and determining of the line between what can be controlled and operated inside the firm and what should be outsourced. This is important because there are significant expenses involved in structuring the fund in such a way whereby most of the activity is in-house.

This setup may be operationally and economically inefficient. Generally, expenses that are internal to the management company may not be charged to the funds; they remain expenses of the manager, essentially eating into potential profitability. Expenses from outsourced
operations can be charged to the fund, increasing profitability for the manager.

The regulatory environment is already burdensome, and will certainly become more complex in the years to come. As a hedge fund evolves, and begins to cross jurisdictionalities, the regulatory environment multiplies in terms of compliance efforts. As such, there is an increasing degree of reliance upon your service providers to keep you up to date on regulatory changes and requirements to assist you, your fund, and your investors in navigating these various regimes.

In the coming years, there will continue to be significant changes. The National Private Placement Regimes (NPPRs) in Europe will essentially discontinue in 2018, as part of the AIFMD. A sizable portion of the industry is currently depending on those NPPRs in order to market their funds to European investors. As the deadline approaches, there will be a shift away from NPPRs, which will require fund managers to engage with service providers and custodians that are able to provide the necessary products and services compliant with the AIFMD.

HFM: How can service providers help hedge fund start-ups meet these operational and regulatory challenges?

AD: Hedge fund managers should seek service providers that not only have the global reach to cover all of the aforementioned topics, but also have sufficient resources available dedicated to keeping abreast of regulatory shifts. From our perspective, being part of a large multinational banking organisation allows us to build, invest in and depend upon our alternatives infrastructure across the globe, so we can bring market-specific expertise and thought leadership to our clients.

As an administrator and safe-keeper of client assets, we can help mitigate risk, ensure regulatory compliance and maximise operational efficiency. This allows the fund manager to focus on portfolio management, and provides hedge fund investors with sufficient comfort that a global bank is independently reviewing and administering the fund.

HFM: What roles does the hedge fund administrator play in the life cycle of a hedge fund, from start-up through launch and beyond?

AD: This has evolved over the last several years at a quickening pace. A decade ago, the HFA was sometimes thought of as a 'necessary evil', whose only existence was to strike NAVs and process investor subscriptions and redemptions. Today, HFAs are climbing the hedge fund value chain. The role of the administrator has become so much more, typically well beyond simply being the accounting and transfer agent of the fund.

Administrators are increasingly being called upon to help navigate regulatory challenges and ensuring compliance with a host of regulatory requirements, such as Fatca, the AIFMD, CFTC, NFA and SEC reporting, while co-ordinating audits and operational due diligence and providing enhanced middle-office products. These are all things that generally form a well-designed service package that a bank or administrator is able to offer a fund and manager. Even at the start-up phase, administrators can offer valuable expertise to fund managers with respect to structuring vehicles; providing insight on distribution; offering regulatory guidance; and advising on target operating models, platforms and the selection of service providers best suited to meet the needs of the fund and its investors.

HFM: What are the most significant changes that technology has brought to the hedge fund industry and can you highlight the importance of striving to follow its constant evolution?

AD: First, as funds and their portfolios become more complex, middle-office services and the supporting technology are increasingly important. This is especially true for funds operating with multiple prime brokers and counterparties. Middle-office solutions enable the administrator to efficiently manage the ‘post-trade’ operations lifecycle and relieve the manager from building or buying technology solutions themselves. Administrators depend upon continuous investment cycles to keep pace with evolving industry demands and the enhanced reporting requirements of investors and regulators alike.

Second, additional platforms related to risk and performance analysis and reporting are becoming more prevalent, as investors seek an independent view into hedge fund investments. Historically, investors were satisfied relying on the risk systems and reports produced within hedge fund firms, but now demand is evolving and they are requesting independent calculation, analysis and reporting for portfolio performance and risk statistics. This is another area where administrators have increased their technology investments.
As measured by the S&P 500 index, dividends included, the market was up by 1.4% in 2015

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Jeffrey Rosenthal (JR): The first year is incredibly important. It creates the first impression of your fund and your abilities for investors. Raising capital is one of the most challenging aspects of starting a hedge fund, and if you are not performing well in that first year, it will be even more challenging going forward. Carefully considering the right time to launch the fund is also essential.

There are several things that should be considered at the onset of hedge fund set-up. One of the very first priorities should be to establish, with absolute certainty, that a hedge fund is the right vehicle for what you want to accomplish. There are many factors and nuances to consider, and gaining a thorough understanding of the financial services space, and the demands and regulations of each option that exists is necessary to understand whether a hedge fund is the most effective tool.

Once that is confirmed, a carefully considered budget should be established, factoring in management, overhead expenses, and what is needed to maintain a reasonable quality of life during the start-up phase. Your instinct may be to take on more responsibility instead of establishing a solid team right away. Keep in mind that the more your time is consumed by management tasks, the less time you have to dedicate to the fund portfolio.

HFM: What do your clients look for when building an initial hedge fund team?
JR: Our clients look to evaluate which key players are most needed for their fund and add people that will bring the most value. They decide upon the right time to expand, and hire the most crucial people first. Starting off, many funds need an analyst almost right away. They prioritise their additional needs, such as when to hire an investor relations manager, CCO, CFO or COO, and often lean towards someone who will wear multiple hats. Look for someone who can help long-term and become a true partner in the fund’s growth.

HFM: What is a feasible amount to raise before launch?
JR: When raising money, it’s important to think about how much you would feel comfortable requesting from investors. Keep in mind that investors may counter with a lower number, and after your meeting is over, their verbal commitment may not materialise. Establish ways to differentiate yourself from other funds, making your pitch more memorable to investors.
HFM: How should a manager differentiate their hedge fund from the competition?
JR: There are so many new funds being launched that differentiation is pivotal. When explaining to investors, keep it simple and straightforward so that they understand your trading philosophy and methodology. Recognise what your strengths are and explain them. Many start-up funds believe that their strength is simply trading securities. It helps to surround yourself with the proper personnel to help you meet your goals, showing investors that you have equipped yourself with what it takes to succeed.

HFM: Is it important to have a long-term concrete goal, or more versatile short-term objectives? Why?
JR: Ideally, you want to have a combination of both. Long-term objectives are crucial. With the high initial costs of starting a hedge fund, you will want that fund to grow and attract assets for some time. You also need short-term goals, such as raising the capital necessary to launch, and deciding upon the right time to expand the team.

Additionally, keep in mind that short-term actions can help with long-term goals. While registering with the SEC isn’t necessary until the fund reaches $150 million, by adopting best practices for compliance beforehand, you are setting yourself up to achieve that benchmark and have an easier time once you’ve arrived at it.

HFM: What are some commonly overlooked aspects that could be put in place upon start-up?
JR: Many start-up funds concern themselves primarily with the short-term picture, but there are a few things that can be set up for long-term success. For example, considering compliance early on, though not required until the fund is registered with the SEC, will make the transition easier, as the procedures are already in place. Also, in the short-term, many funds choose the most cost-friendly service providers. However, acknowledging early on that as the fund grows, service providers with more specialised knowledge may be necessary can be a huge advantage. Starting the research and opening up the conversation with service providers who know the hedge fund space can translate into sound advice as your fund grows. Contrary to popular belief, it’s never too early to be thinking about infrastructure. Decide what your needs are and at what point in your growth you would like to hire a CFO, client relations, marketing, etc.

HFM: Are there any missteps that you see occurring that can be avoided?
JR: One trend that I’m seeing is a dramatic change of strategy if returns are not as good as expected right away. From what we’ve seen with our clients, the ones who maintain their convictions and continue to push their strategy through the initial bumps in the road have greater long-term success. Of course, there are no guarantees, but we encourage our clients to determine early on what outcome would cause them to abandon or change their strategy.

HFM: Is the process of starting a hedge fund becoming easier or more difficult?
JR: The process has undoubtedly become more difficult. There is so much competition between new funds, larger, more established funds, and even day traders, often resulting in many people chasing the same ideas. Also, the regulatory process has gotten more complex, compliance costs have increased, and the act of complying with regulations has become more involved and time-consuming.

The level of investor due diligence grows more and more extensive, and patience from investors tends to grow thinner. Funds would ideally have time to show returns, prove their growth strategy, and expect their investor to remain with them through a certain degree of volatility, but this rarely appears to be the case anymore. Investors seem quicker to pull capital from funds at typically the worst times, which can create a domino effect where you have to liquidate positions to make redemptions.
When everything looks complicated the answer is as simple as one

About Opus Fund Services:
Formed in 2006, Opus Fund Services is a premier, award winning independent fund administration firm providing automated, integrated middle and back office administration services to domestic and offshore hedge fund and alternative investment vehicles.

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HEDGE FUND FIRST STEPS

JOSEPH CASSANO, AUDIT SENIOR MANAGER AT WITHUMSMITH+BROWN, DISCUSSES
THE INITIAL STEPS AND KEY CONSIDERATIONS OF STARTING A HEDGE FUND

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here are many reasons why starting a hedge fund is a hot topic. The term ‘hedge fund’ is mentioned daily throughout various media outlets. Prior to Dodd-Frank, it was relatively easy to launch a hedge fund with minimal capital; however, as regulations have become more stringent, the industry has seen a push for bigger and better infrastructure, including implementing risk controls and hiring more personnel within hedge fund back offices to create levels of checks and balances. Hedge funds that raise capital over $150m in assets are now required to register with the Securities and Exchange Commission. As a result, there will be a significant increase in expenses.

In addition, investors are demanding longer track records along with positive performance, which has driven up the time necessary to fundraise. Some hedge funds will launch with either their own capital or subscribe to a friends’ and family-only approach in order to obtain a track record on returns to attract outside unrelated capital.

Hedge fund launches exceeded fund liquidations during 2015. A significant reason for this in the past year is we have seen prominent managers spin out of reputable firms and attract hundreds of millions of dollars in new capital. We are currently at a record number of hedge funds despite recent disappointing performances, as they offer investors more attractive risk to adjusted return potential than your traditional investments.

When looking to launch a hedge fund, there are a multitude of factors that will decide how successful the alternative investment will become. Hedge fund managers will need to have a plan in place to address these factors.

WHERE IS THE MAJORITY OF MY CAPITAL BASE COMING FROM? WHO AM I TARGETING?
It is important to develop a plan for raising capital before starting up the hedge fund. There are many potential sources for investor capital, which include your personal network of family and friends, seed-capital providers, hedge fund of funds, endowments and foundations, pensions, and high-net-worth individuals (HNWIs).

Hedge fund launches that are on the smaller side tend to develop plans that turn to one of the following three methods of capital raising: utilise resources from family and friends, market to HNWIs and cultivate a long-term affiliation with seed-capital providers. New launches will normally have to utilise some combination, if not all three, of these methods for fund raising.

WHAT SETS YOUR HEDGE FUND APART FROM OTHERS? IS IT THE STRATEGY?
Hedge funds that are in their infancy stage should not take for granted the importance of clearly defining their investment strategy and how it will be communicated to potential investors. Will the fund use a similar strategy to other established hedge funds or will it develop a new algorithm for black-box trading? Hedge funds should always know who their direct competition is regarding investment strategy and should identify what sets them apart from the competition. A prudent start in strategic planning is maintaining a list of competitor hedge funds that have similar strategies and know what sets your hedge fund apart.

HOW LARGE DO YOU WANT YOUR ASSETS TO BE?
It is important to understand the amount of assets your hedge fund can manage to become profitable and the demand for risk controls as well as the cost associated with them. Some items that directly affect profitability are the size of the back office team needed in order to have proper internal controls in place. Smaller hedge funds with friends and family capital will try to minimise cost and overhead to maximise returns. Hedge funds that strive to appeal to institutional investors will typically want a more robust back office and a deeper level of control and review.

WHO ARE THE RIGHT SERVICE PROVIDERS?
Selecting the right service providers such as administrators, brokers, attorneys and auditor for the size and complexity of your hedge fund is imperative to ensure a smooth and efficient operation. Each of the service provider selections should be seen as an investment in the longevity of the hedge fund.

Hiring an experienced hedge fund attorney from the initial start of a hedge fund is vital to ensure compliance with the ever-changing landscape of the alternative investment universe. They will prepare the hedge fund documents correctly and assist in avoiding regulatory snags.

Hedge fund managers should select a prime brokerage firm as an integral part of how the hedge fund trades and operates. This should be a well thought-out decision weighing the costs and benefits of doing
business with various brokerage firms. It is in the hedge fund’s best interest to partner with a brokerage firm that is motivated to serve its needs and is familiar with the investment strategy of the fund. However, the fund should make sure the brokerage firm is sizable enough to meet all the required trading and brokerage needs.

The first step in choosing a fund administrator is deciding what functions will be done internally and what will be outsourced. The hedge fund should analyse which fund administrators are a good fit for their needs and factor in their reputation in the industry. The next steps a hedge fund should take are to examine whether each administrator has the right technology to meet the hedge fund’s trading strategy. At this point, it is a good idea for the hedge fund to perform their due diligence by speaking to some of the administrator’s clients, both those that are similar in size and strategy to the fund and those that are different. By doing this, the hedge fund will get a realistic picture of how the administrator performs and deals with various clients.

Engaging an audit firm can be a daunting task since there are many audit firms across the United States that offer audit and tax services for hedge funds. Going with a ‘Big 4’ accounting firm can offer name recognition to hedge funds looking to appeal to institutional investors; conversely, choosing these firms regularly comes with a higher price tag that is not always appealing to a start-up hedge fund and can be a significant expense against hedge fund performance. Start-up hedge funds typically find themselves in the middle-market audit firm arena, which features significant experience and knowledge of the industry, affordable costs, and more personalised services in relation to the larger firms.

Ultimately, new hedge funds should choose an audit firm that has substantial industry experience and knowledge, superior client service, and a good reputation within the alternative investment industry. The hedge fund should meet with all members of the engagement team with whom it will be working to understand the depth and expertise at each level.

Launching a hedge fund is a multi-year commitment to developing the hedge fund strategy, building the right team and support system, and finding the right niche where your hedge fund can operate profitably. The most important factor is performance. Good performance will always drive capital into a hedge fund. Putting the above plan into place allows the hedge fund manager to focus on what they do best, trading investments.
Sadis & Goldberg represents over 600 hedge and private equity funds. Above all else, we value our client relationships. Our attorneys strive to provide excellent, consistent, practical and efficient legal services. We distinguish ourselves from other law firms by assisting our clients in the development of their businesses. This comprehensive approach has often earned us recognition as one of the top five law firms in the U.S. for our hedge fund practice. Invest a few minutes to learn what our attorneys can do for your business.
SOLUTIONS FOR AND BEYOND THE START-UP STAGE

PALAK PATEL, GLOBAL HEAD OF PRODUCT DEVELOPMENT FOR BLOOMBERG’S ASSET AND INVESTMENT MANAGER (AIM), TALKS TO HFMWEEK ABOUT HOW CHOOSING THE RIGHT SERVICE PROVIDERS CAN HELP FUND MANAGERS MEET CHALLENGES THROUGH DIFFERENT STAGES OF THEIR FUND’S GROWTH

HFMWeek (HFM): What are some of the biggest challenges that face a manager looking to start a hedge fund?

Palak Patel (PP): When you look at the backgrounds and expertise of the managers that are starting hedge funds, generally, these are people whose experience includes picking stocks, managing portfolios and managing risk. All of a sudden they are faced with challenges such as picking office space, making sure they have network communications, ensuring they implement the right technology and hire the right people to help them raise capital. There is a myriad of operational challenges that a start-up hedge fund has to face, and often managers have little experience of dealing with these operational hurdles.

What we are doing at Bloomberg, is helping start-up fund managers with the operational challenges and investment challenges they are going to face. In addition to helping managers check all of the boxes on the technology and operational side of running their business, we are also providing tools that help them make timely and accurate investment decisions.

Building the technology infrastructure to support a new hedge fund’s trading strategies and operations can be a daunting challenge, so managers must be highly selective when they choose technology partners.

There are a number of different technology vendors out there that help people solve very specific challenges that managers are likely to face. But then there are technology partners like Bloomberg that are uniquely positioned to solve a number of different problems.

It is extremely important to choose the right technology partner that is going to scale with the fund as it grows its operations. When you start off with, for example, $25m-$50m, you have a set of challenges. But as you grow and you are managing closer to $100m up to $1bn, the level of transparency of your operational control required by investors increases. Working with the right technology partner from the beginning can make a big difference for start-up funds. Establishing the right technology foundation and working with the right team of people allows managers to focus on their mandate and leave technology issues to their technology partner.

Attracting capital is another fundamental challenge. However, fund managers who can demonstrate they have invested in a robust infrastructure to support their compliance, operations, and reporting can position themselves at a distinct competitive advantage.

Often clients come to Bloomberg looking for an operational tool and a technology tool. But one of the things they also get with Bloomberg is the benefit of our community. The diverse community on our system and the events we host provide opportunity to discuss capital and investment challenges with colleagues throughout the industry.

HFM: How can a new hedge fund best handle all of the demands from current and pending regulations?

PP: Achieving regulatory compliance is paramount for any asset manager, but can become more difficult when you have deficient technology resources or a piecemeal approach to addressing all of your requirements.

In addition to having the right technology that is going to help hedge fund managers comply with regulation, it is also important to have a technology partner that has the resources to keep up with regulatory change. At Bloomberg we have operations in the Americas, Europe and Asia. With these operations comes well-resourced regulatory teams. These teams not only help our Asset and Investment Manager (AIM) business, but help us understand what changes we need to make to our order and execution management solutions, electronic trading platforms and our analytics and data offerings. We benefit internally from that scale, but in turn, our clients benefit from the fact that we have a presence in almost every jurisdiction we operate in. We can ensure their technology is able to keep up with regulatory change, as well as helping them understand the changes that are going to impact you in the future.

It is important to take a holistic approach to compliance requirements. This holistic approach comes from the realisation that client’s requirements are likely to change as they grow or enter new asset classes, strategies or markets. Their technology should support the full spectrum of needs such as pre-and-post-trade compliance, audit trail reporting, transaction cost analysis and message archiving so that they can have confidence that all their bases are covered.

HFM: What is Bloomberg offering to hedge fund start-ups?

PP: Bloomberg offers a suite of solutions for start-up funds that provides them with a solid technology foundation
so they can handle day-to-day trading and compliance activities. These solutions are designed to be scalable and flexible to accommodate future growth.

We aim to help start-up funds simplify investment operations, reduce operational risk, and minimise up-front infrastructure costs and long-term overhead. These are the things that all funds need to consider, but are especially important to funds in the start-up phase.

For start-ups, Bloomberg’s AIM product provides multi-asset trade execution, portfolio management tools, operations and regulatory compliance functionality. Our compliance tools provide real-time pre-trade, post-trade and end-of-day monitoring for client, firm and regulatory requirements. They include advanced rule building, reporting and complete audit history, ability to monitor and investigate trades and evaluate performance to ensure compliance with best execution, mandates and authorised counterparties and stocks, as well as conduct surveillance to monitor adherence to regulations.

On the execution side, clients have access to our vast order routing network, and deep integration with our electronic trading systems including a market leading Execution Management System in EMSX. From an operations perspective, we provide out of the box connectivity to multiple prime brokers and fund admins as well as reconciliation tools. We give funds the tools required to ensure accurate position data, allowing managers to make investment decisions from a single screen.

**HFM:** How does your offering differentiate itself? What can Bloomberg provide a start-up fund that other technology providers cannot?

**PP:** Bloomberg offers a unique suite of capabilities for start-up funds that are largely delivered through Bloomberg’s desktop, which fund managers and traders are generally already familiar with, or as an auxiliary component. However, to the hedge fund manager, we are delivering everything they need in an integrated fashion and through a single point of contact so they do not have to deal with multiple vendors and technology solutions that are not compatible. The suite of services includes professional-grade technology with a fully managed, hosted infrastructure backed by a global service and support team.

Even though we do not provide a consulting service, we deliver our solutions with a consultative approach. Our staff has experience of covering hedge funds of all different sizes that trade across all different asset classes and have different trading strategies. Our clients have the benefit of being serviced by experienced staff, in a manner that is beyond the standard, transactional approach.

One of our key strengths is our integration with the Bloomberg Professional service, or terminal, and the community of professionals that exist on the terminal. This provides access to our communication tools and our other community tools combined with diverse liquidity pools across multiple asset-classes. This combination is a key differentiator for us in the market.

In addition, Bloomberg offers a fully hosted platform, so there are no servers to manage or upgrade. Our platform includes disaster recovery, mobile access and FIX connectivity to defined prime brokers and fund administrators.

What also must be taken into account, is the integration of news and event information into our workflows. Through the Bloomberg Professional service, hedge fund managers have access to the data, news and analytics relied upon by a community of over 325,000 subscribers globally.
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Opus Fund Services

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Sadis & Goldberg LLP

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