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# A Hedge Grows in San Francisco

## Founders of West Coast Hedge Fund Practice Are Leaders Today

**By Anna Oberthur**
Daily Journal Staff Writer

S. TODD ROGERS / Daily Journal

Douglas Hammer, from left to right, Carolyn Reiser, Christopher Rupright, Neil Koren, Geoffrey Haynes and John Broadhurst work in Shartsis Friese & Ginsburg's hedge fund group. They counsel more than 500 clients.

The year was 1983, and John Broadhurst and Douglas Hammer were pretty sure they were onto something.

The attorneys were busy practicing corporate and securities law at Shartsis, Friese & Ginsberg in San Francisco when a client who wanted to start a hedge fund approached them.

At that time, such investment vehicles — and attorneys to represent the money managers — were rare on the West Coast.

Although he knew little about the subject, Hammer did some quick research and helped the client. Shortly afterward, the phone started ringing; other money managers were looking for attorneys, too.

"You get three or four of these calls, and all of a sudden you scratch your head and say, wait a minute, what's going on here? Is this a trend?" Broadhurst said.

He soon realized he was looking at a major business opportunity.

"I jumped on it with both feet," Broadhurst said during a recent interview. "I decided I was going to really attack this sector."

Broadhurst flew to New York, where hedge fund practices were more established. He phoned the top attorneys in the specialty there and asked them to lunch.

"I said I was the West Coast hedge fund guy — having done three," Broadhurst said. "And we got ourselves known back there as a West Coast firm that specialized in the area."

At that time, there probably were not more than 100 hedge fund managers in the country, and few West Coast attorneys with significant knowledge of the burgeoning trade, the lawyers estimated.

Broadhurst and Hammer began attending conferences, meeting industry leaders, training associates and researching the practice issues — taking the steps to carve out a niche that would become what today is widely regarded as one of the top investment advisory groups in the country.

With 12 attorneys — including five partners — spending most or all of their time on investment advisory work, the practice is considered the largest of its kind on the West Coast. They estimate they counsel more than 500 clients.

The group represents investment advisers in all aspects of their businesses, but it focuses about 70 percent of its time on hedge fund managers.

That work is geared toward helping managers set up new funds, giving guidance on regulatory issues and standard business issues such as new hires, and, if necessary, giving counsel during a SEC investigations.

An increasingly popular means of investment, a hedge fund is an investment pool that has a performance-based fee and the ability to short sell. Investors typically are high-net-worth individuals and institutions, and the manager often has a significant part of his own money invested in the fund.

As of January 2005, more than 8,000 hedge funds represented more than $934 billion in capital worldwide, according to the Hennessee Group, a New York organization that tracks the industry. That number has climbed steeply since 2000, when total holdings were a relatively modest $324 billion.

Ironically, that popularity is indirectly due, at least in part, to the funds' higher visibility, a byproduct of increased news media attention that stemmed from the recent Wall Street scandals.

The hedge fund business, Hammer said, has gotten more press over the last few years than in the previous 15.

"It's the flavor of the month," Broadhurst said. "When you look at it, it's all over the newspaper."

Hedge funds hit the regulatory radar screen in the late 1990s, when the multibillion-dollar Long-Term Capital Management fund tanked, nearly dragging down the nation's banking system with it, Hammer said.

Then, in 2003, hedge funds got caught up in the market-timing scandals unearthed by New York Attorney General Eliot Spitzer. Managers from several prominent hedge funds settled with Spitzer's office or pleaded guilty after being accused of fund-related wrongdoing.

"That put another black mark on hedge funds," Broadhurst said. "You had thousands of these things being formed, and the SEC started saying, 'We want to figure out what these are.'"

Citing concern for the protection of investors and the suppression of fraud, the SEC last year adopted a regulation requiring hedge fund managers running more than $30 million to register with the commission.

The commission noted in the July 2004 rule proposal: "Unregistered hedge fund advisers operate largely in the shadows, with little oversight. ... While these conditions can stimulate a tremendous amount of investment creativity and profit, they are also a perfect medium for the germination and growth of frauds."

The rule, which the attorneys expect will make it more costly to start a fund, is scheduled to take effect in February 2006.

The Shartsis attorneys worry the rule could have a chilling effect on new funds. Hammer suggested the SEC's action could have been politically motivated.

"Spitzer is getting all of these headlines the SEC figures it ought to be getting," he said.

If — God forbid, Hammer said — the SEC comes knocking on the door of one of the firm's clients, the firm has four former SEC enforcement attorneys ready to advise.

While most of their clients are serious investors with their own money in the funds, the attorneys say they have seen a few "gunslingers" whose funds quickly blew out, especially during the dot-com boom.

"They weren't properly hedged," Hammer said. "They weren't thinking about that. They were just trying to hit a home run. And they swung and missed."

Even responsible fund managers can blow it, given the risks involved, the attorneys said. One client started three hedge funds in 1999, investing $60 million dollars in the Internet — and then lost all but $5 million in the course of a year.

"So he just closed up," Hammer said. "He quit and shipped his SUV over to China," where he planned to drive across the country. "I don't know what happened to him. Great guy, but his timing was bad."

All this makes for an interesting and busy practice.

Shartsis, with 50 lawyers in a single office, names as its competition some of the biggest law firms in the nation: Ropes & Gray; Paul, Hastings, Janofsky & Walker; Kirkpatrick & Lockhart Nicholson Graham; Howard, Rice, Nemerovski, Canady, Falk & Rabkin; and Schulte Roth & Zabel.

"Clearly, when you're looking into San Francisco hedge fund practices, they are, without a doubt, the finest local example," said Gregory Sheehan, chairman of Ropes & Gray's investment management group in Boston. "They've focused very hard on this area, and they have terrific lawyers."

Sheehan said Ropes & Gray has three attorneys in San Francisco who do investment management work, including hedge funds and mutual funds. He said he'd like to see the group grow to 10 attorneys.

"Everybody is just pressed to the gills with work," he said.

The Shartsis group has been a major contributor to the success of the hedge fund industry in the Bay Area, said David Sung, who leads Ernst & Young's asset management practice in the Pacific Northwest.

"In my mind, they are the Tiffany of the law firms," Sung said.

One of the keys to the practice's success has been the firm's commitment to providing clients a heavy dose of partner time, the attorneys said.

"That's sort of our market approach: excellent service, great work product and heavy partner involvement," Broadhurst said.

Clients also appreciate being able to call the firm and reach a dozen qualified attorneys, plus the firm's tax partner Geoffrey Haynes, who works part time on investment advisory issues.

> **'You learn it by hook and by crook. And that's just more interesting than picking up the horn book and flipping to page 182."**
>
> **Christopher Rupright,**
> Shartsis, Friese & Ginsburg partner

"It's a remarkably successful group," said Art Shartsis, who co-founded the firm in 1975.

But firms have traditions and cultures, and Shartsis is service driven, client oriented and absolutely committed to quality, he said.

"We have the highest standards and we get the best people," he said.

There's also a strong commitment to encouraging lawyers to expand their own practices.

"We rely a lot on the initiative of the individual," Shartsis said. "We try not to second-guess people's judgment. John [Broadhurst] tells us he thinks it's a good practice opportunity; we do whatever it takes to support it."

That attitude has helped the firm draw talent to the practice group.

Partner Carolyn Reiser, who joined Shartsis in 1993, said it's one of the elements that attracted her away from Morrison & Foerster.

"It's much more entrepreneurial," Reiser said. "I liked Morrison & Foerster, but I thought, long term, the potential to really have my own practice, to be sort of the master of my own fate, was stronger here."

Reiser said she finds it odd that more attorneys aren't doing investment advisory work.

"It's a very appealing practice," she said, a little arcane and technical, but intellectually interesting. "It's a practice that lets you really develop your relationship with your clients in a kind of outside general counsel mode. So you see a wide range of issues."

Partner Neil Koren joined the group in 1999 after practicing hedge fund law at Schulte Roth in New York. That firm is thought to have one of the largest hedge fund practices in the country.

He said he enjoys working with the hedge fund managers.

"They're very entrepreneurial, very smart and very motivated," Koren said.

At Schulte Roth, he said, Shartsis' hedge fund practice was highly regarded. When he wanted to move to San Francisco and continue working on hedge funds, Shartsis seemed the perfect fit.

"It was thought of as an extremely high quality group and one of the national leaders of hedge fund lawyers," Koren said. "They sort of recognized Shartsis as a peer."

The Shartsis group's fifth partner is Christopher Rupright. The hedge fund law practice is unusual, he said, because so much of it remains to be interpreted.

"You learn it by hook and by crook," Rupright said. "And that's just more interesting than picking up the horn book and flipping to page 182."

Elizabeth Foster is a partner at Kilkenny Capital Management. Broadhurst helped establish the investment group 11 years ago in San Francisco and continues to serve as its general counsel.

Although Kilkenny now has offices in New York and Chicago, where Foster is, she said it has never considered switching counsel.

"We have no interest in using any of the bigger names," Foster said.

According to hedge fund attorney Mark Whatley of San Francisco's Howard Rice, any investment advisory attorney's success depends on understanding the client's needs. Clients don't necessarily know the right questions to ask, and they need guidance to navigate the business' technicalities.

"Shartsis developed that capability when the industry was nascent here," Whatley said.

Hammer and Broadhurst "really focused quite intensively on hedge funds and just built a heck of a business," he added.

At Howard Rice, five attorneys do hedge fund work more or less full time - although Whatley is the group's only partner. The firm wants to expand the practice, Whatley said, but it's difficult in the Bay Area to find the top end attorneys they want.

Kirkpatrick & Lockhart also plans to bulk up its practice in San Francisco. The firm has 70 attorneys who do various kinds of investment management work nationwide, including Mark Perlow and three other partners in San Francisco who do hedge fund work.

New work stemming from the increased SEC scrutiny, plus the fact that the San Francisco market is underserved, make the Bay Area a good place to build a hedge fund practice, Perlow said.

"Hedge fund managers have found San Francisco to be a very conducive environment," Perlow said. "We're very optimistic" about the local practice.

As strong as Shartsis' practice is, though, management is cautious about over expanding.

"We grow it very slowly because we are completely committed to the quality of the practice," Shartsis said.

Still, in the age of massive mergers creating firms with thousands of attorneys, it's worth asking whether Shartsis, tiny by comparison, will need to expand in order to compete.

There are some advantages in the practice to having access to people all over the world, Shartsis conceded.

On the other hand, he said, for attorneys, a sense of self-determination is lost in megafirms, he said.

"There's a certain pride in the firm that we compete very favorably with firms 20 to 30 times our size," Shartsis said. "It's clear big has become a premium, and whether that's the right premium, I don't know.

"Everybody's changing. Whether we change or not, who knows."

■ E-mail: anna_oberthur@dailyjournal.com