

# Perspectives+

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## Managed Accounts: Panacea or new source of risk?

In the wake of recent events, and as a reaction to a change in investor sentiment, managers are beginning to embrace the managed account model

*In this edition of Perspectives, Christopher Rose, founder and CEO of Clear Lake Consulting, has contributed his expertise on managed accounts. To find out more about Clear Lake Consulting, or to contact the author directly, click [here](#).*

There are few investors who were not caught by the lack of liquidity and transparency in their holdings in 2008. Solutions are needed, and it is clear that Managed Accounts can help address these issues, as well as the more publicized fraud concerns that kept the media so busy in 2008.

Despite being around for more than a decade, hedge fund managed accounts represent less than 2 percent of the hedge fund market. The biggest historical impediment to their widespread use has primarily been a general

reluctance on the part of the manager to utilize this type of structure due to higher costs and increased operational requirements. But in the wake of the events of 2008, and as a reaction to a change in investor sentiment, managers are beginning to be more willing to consider the managed account model. A recent Deutsche Bank study highlighted the fact that 43 percent of investors are now considering making investments through managed accounts. This, along with public commitments by CALPERS and other large institutional investors to managed accounts, is causing a shift in the hedge fund industry.

### Managed Accounts: A Definition

Broadly defined, a managed account is any vehicle in which an *(continued on page three)*

## LaCrosse and Ocwen announce partnership, introduce LaCrosseMortgage+™

New back-office solution offers fund administration services and industry-leading real estate expertise in loan servicing and valuation

LaCrosse Global Fund Services and Ocwen Financial Corporation recently announced the introduction of a specialized suite of services available to investment funds investing in U.S.-based loans, mortgages and distressed assets. Ocwen will provide seamless integration of its innovative mortgage servicing and valuation offerings to customers of LaCrosseMortgage+™, a specialized fund administration and middle-office support package for investment funds that trade in whole loans.

Rapid growth in fund structures aimed at investments in commercial mortgages, residential mortgages, mortgage-backed securities and related derivatives requires increasingly high levels of service requirements in the real estate arena. To meet this need, the new partnership offers a complete back-office solution that includes fund administration services and progressive real estate expertise in loan servicing and valuation. LaCrosse and Ocwen will work together to develop solutions to meet clients' specific needs in these areas. *(continued on page four)*

## LaCrosse Global Fund Services Joins Forces with Hedge Fund Industry to Launch Hedge Funds for Habitat – UK

Hedge Funds for Habitat-UK, an initiative by the hedge fund community, has launched a campaign to support Habitat for Humanity. The charity, which works in over 90 countries, enables people living in poverty housing to access a safe, decent home in which to live.

Building on the success of "Hedge Funds for Habitat – NYC", "Hedge Funds for Habitat - UK" is helping to globalise the hedge fund community's support for Habitat for Humanity by participating in an inaugural UK event called the Hope Challenge. The event, which took place June 12-14, 2009, is a team challenge that involves 20 miles of trekking, 1,000 meters of hill ascent, and the team spending the night in a shelter they construct themselves from scrap materials. The fundraising income from the event will go to Habitat for Humanity's projects in the developing world. The Hedge Funds for Habitat - UK team, consisting of supporters from LaCrosse and Black River Asset Management, performed well, taking second place in the competition and first in fundraising among financial service providers.



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**"Safe, decent and appropriate homes will help families to thrive, and that helps all of us to flourish."**

**Stuart Feffer**  
co-Chief Executive Officer  
LaCrosse Global Fund Services

"It costs an average of just £1,235 to provide a family in the developing world with a safe, decent place to live," said Stuart Feffer, co-chief executive officer of LaCrosse Global Fund Services, one of Hedge Funds for Habitat-UK's founding partners. "Hedge Funds for Habitat-UK is calling on supporters from hedge funds, private equity firms and the service provider community to support us in our goal. Hedge fund professionals know that investing in human capital is key to the success of our industry – and our cities. This applies equally, if not more so, in the developing world. Safe, decent and appropriate homes will help families to thrive, and that helps all of us to flourish."

"Over 2 billion people worldwide live in poverty housing, which causes insecurity and poor health and consequently limits their ability to earn an income," says Ian Walkden, national director of Habitat for Humanity - GB. "This, in turn, means they cannot pay for healthcare or education, and so they continue to be dependent and vulnerable from generation to generation. Enabling access to a safe, decent place to live can break this cycle. We are really excited about this unique collaboration with LaCrosse Global Fund Services and the UK's hedge fund industry. Hedge Funds for Habitat-UK unites global hedge fund leaders—among the most innovative thinkers and doers in London and environs—with an innovative housing initiative that addresses one of the most pressing problems in our world today."



Habitat for Humanity works at the grassroots level in communities affected by poverty housing, offering a hand up rather than a hand out. Typically, the community provides both the people to scope and manage the project and the volunteers, including those who will live in the homes, to help build or renovate. Habitat for Humanity provides access to training, funding and a worldwide network of expertise. It empowers the community to be its own solution to its local poverty housing issues.

Hedge Funds for Habitat-UK is dedicated to assisting Habitat for Humanity in its efforts to help people escape from poverty housing. To contact, learn more or make a donation, please visit <http://www.justgiving.com/hedgefundsforhabitatuk>.

### About Habitat for Humanity – UK

Habitat for Humanity was founded in 1976 with the aim of eradicating poverty housing and homelessness across the globe. Using donated money, materials and volunteer labour we work in partnership with people in need of shelter to build safe, decent homes in over 90 countries around the world. Today we have helped over 1.5 million people in more than 3,000 communities to begin a new future full of hope.

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## ...Managed Accounts (continued from page 1)

investor directly owns a pool of underlying assets that an investment advisor manages on a discretionary basis. The manager's role is generally limited to the right to make investment decisions. This differs from a traditional hedge fund in which an investor is part of a commingled pool, and the hedge fund manager has broad control over the assets of the fund being managed.

- + There are two fundamentally different types of managed account structures: the separately managed account (SMA) and the single investor fund. The SMA mimics the separately managed account of the long-only world in which an investor opens accounts with custodians/prime brokers and employs managers as advisors to make investment decisions on their behalf. By contrast, the single investor fund approach looks more like a traditional hedge fund structure in which an investor sets up a special purpose fund vehicle sub-advised by the hedge fund manager in which it remains the only outside investor (the fund manager may carry an ongoing interest in the fund as well, typically through earned performance fees that remain invested in the vehicle).

### Managed Accounts: The Benefits

The primary impetus for the accelerated shift to managed accounts has been a desire to mitigate fraud, liquidity and transparency risks seen as inherent to the existing hedge fund model. By moving control of assets away from the hedge fund manager, having them custodied separately with direct control by the investor, the managed account approach can help reduce these risks. Other benefits of the managed account approach include increased transparency and the potential to liquidate assets on the investor's terms.

### Managed Accounts: The Challenges

There are some major challenges of adopting managed accounts. The root cause of these challenges is the structural change inherent in managed accounts. By shifting control over assets from the hedge fund manager to the investor, significant responsibilities are also shifted. This shift creates many new risks that need to be managed by the investor and significant costs.

In the traditional hedge fund approach, the hedge fund manager controls all of the functions needed to operate a hedge fund. Beyond portfolio management, these include valuation, accounting, collateral management and operational support for derivatives and privately placed investments (equity and debt). While traditional hedge funds outsource some of these functions to third parties, in reality the hedge fund manager still retains control over these functions and their smooth integration.

In the managed account model, responsibility for performing these functions sits with the investor, or with service providers selected and managed by the investor. Costs can be significantly higher, as there are no economies of scale from sharing services across a single vehicle with multiple investors, and for smaller managed accounts the associated fixed costs can be high.

Investment advisors face additional obstacles. An example is the need to ensure that all investors, including the owners of any managed accounts as well as investors in commingled funds run using the same or similar strategy, are treated fairly, from an investment and return perspective. This can be especially difficult if managed account holders have the ability to liquidate a portfolio without notice while investors in similar commingled funds do not. Even in highly liquid strategies, this is a poorly understood aspect of any program that can give rise to significant angst between investors, managers and service providers.

In more complex hedge fund strategies, the shift of some functions from manager to investor is even more complex, particularly when the strategy involves use of OTC derivatives (where the investor directly, rather than a fund vehicle, may now be the counterparty, and where the investment advisor must establish trades separately for each managed account).

### Managed Accounts: Emerging Solutions

Another approach to managed accounts, the Separately Managed Account Platform (SMAP), is beginning to emerge. In a SMAP, a platform operator provides a common platform and operational infrastructure with a more open architecture, offering accounts managed by a number of investors using common custodial and administrative arrangements. The platform provider manages any other service providers used and reduces the expertise and manpower needed by the investor.

Regardless of the type of solution adopted, investors must have a good understanding of the managed account approach before embarking down this path. They also need to understand what will be required of them in establishing and overseeing the program. This effort may not be a huge undertaking, but it can be a challenge for anyone unfamiliar with the way these programs should work. The challenge is compounded by the fact that *(continued on page four)*

## ...Managed Accounts (continued from page 3)

the managed account space is immature, such that there are few industry professionals with real experience of constructing or operating these programs successfully.

### In Conclusion

Managed accounts are fast becoming a major component of the hedge fund investment space. They offer the potential to address most of the pressing problems inherent in the current hedge fund model, but they are not a panacea. Unlike the parallels in the traditional investment space, they require a very significant change in approach from both an investor's and a manager's perspective. This introduces significant new risks to be mitigated and costs that must be borne.

### About the author

Christopher Rose is the founder and CEO of Clear Lake Consulting, a hedge fund consulting organization with a specific focus on hedge fund managed accounts. Prior to founding Clear Lake, Chris was an early pioneer in the managed account space as the architect, Chief Technology Officer and Chief Operating Officer of an independent commingled Managed Account Platform with approximately 70 hedge fund managers and \$3 billion in AUM allocated across all major hedge fund strategies. Most recently, Chris designed an open-architecture managed account platform (SMAP) providing customized, separately managed accounts for large institutional investors.

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## ...LaCrosseMortgage+™ (continued from page 1)

"Our goal is to take advantage of the recent burgeoning in investment vehicles for purchasing both performing and non-performing mortgage loans. These vehicles have administrative and operational requirements that are often different from typical hedge funds and private equity funds, and LaCrosse has developed unique expertise in servicing this type of investment. Our partnership with Ocwen complements the current operational and administrative support platform that LaCrosse offers to its clients in support of operational best practices," said Stuart Feffer, co-CEO of LaCrosse.

The partnership between Ocwen and LaCrosse responds to the recent market growth of financial institutions being forced to divest distressed and non-performing assets from their balance sheets. As markets and investors have witnessed, the failure to fully understand the complexities of servicing, valuation and exit strategies of these assets by investors has resulted in massive portfolio writedowns and devaluation of pricing.

Specific components of LaCrosseMortgage+ offered by LaCrosse include fund administration for the investment pool and related entities, as well as middle-office and operational support for any securitized or derivatives trading. Services offered by Ocwen as part of this partnership include valuation, due diligence, forensics and a full suite of services to support pre-foreclosure, foreclosure and real-estate owned (REO) assets.

"As the financial markets continue to work distressed assets through the system, it will be absolutely necessary for market participants to fully review, understand and develop the best proactive strategies for managing these complex assets. This partnership provides a set of integrated tools in the fund manager's tool box that they can use in determining, valuing and managing the risk/reward opportunity in this segment of the market," said William Shepro, president of Ocwen Solutions.

## LaCrosse in the News

A roundup of news stories and press coverage on LaCrosse Global Fund Services. Click on the links below to open the articles in your web browser.

- + + July 14, 2009 **FINalternatives** LaCrosse Global Fund Services to Provide Fund Administration Services to Noctua Asset Management's Alto Global Fund, Ltd.
- + + July 2, 2009 **Press Release** LaCrosse Global Fund Services to Provide Fund Administration Services to Tahan Capital Management Pte Ltd. (pdf)
- + + June 24, 2009 **Hedgeweek** LaCrosse Global Fund Services to Provide Fund Administration Services to Flowering Tree Investment Management.
- + + June 12, 2009 **Reuters** LaCrosse and Ocwen Financial Announce Partnership to offer fund administration and industry-leading real estate expertise in loan servicing and valuation.
- + + June 10, 2009 **Opalesque** Opalesque Exclusive: Part One - Has third party administration become a necessity?
- + + April 15, 2009 **Opalesque** LaCrosse Global Fund Services to Provide Fund Administration Services to Numen Capital LLP.
- + + April 15, 2009 **The Hedge Fund Journal** LaCrosse Global Fund Services to Provide Fund Administration and Operations Services to Cavenagh Capital.
- + + Feb. 23, 2009 **Global Custodian** LaCrosse Global Fund Services to Provide Operations Services to Primergy Capital Partners.

## About LaCrosse Global Fund Services

LaCrosse Global Fund Services is an independently managed subsidiary of Cargill, one of the largest privately held companies serving customers worldwide. With 10 global offices, LaCrosse can work closely with a fund's prime brokers and custodians to meet all of its operational and administrative needs. LaCrosse provides support for a wide range of strategies run by global portfolio managers, covering fixed income, distressed debt, structured credit, equities, currencies, commodities and a full range of related derivatives.

LaCrosse began as a spinout of the middle- and back-office operations that had supported Black River Asset Management and, prior to that, Cargill Global Capital Markets. Today it is an independently managed subsidiary of Cargill providing services to the alternative investment industry. For more information, visit [www.lacrosseglobal.com](http://www.lacrosseglobal.com).

To see a complete list of asset classes supported by LaCrosse Global Fund Services, please click [here](#).