



Corporate Governance - The role of directors

The basic duty of directors is to oversee the affairs and activities of the company and to be diligent in representing the interest of shareholders. In practice, the board of directors is responsible for negotiating and overseeing contracts with each entity with whom it conducts business, for example service providers to the fund, and to monitor their performance in accordance with the terms or obligations of the contracts. Taxation, anti-money laundering, compliance related issues will also be in the scope of the directors' responsibilities.

According to the Statement of Guidance issued by the Cayman Islands Monetary Authority (CIMA) on corporate governance, the board of directors should be composed of a balance of appropriately skilled, experienced and qualified individuals who can make informed and independent judgments regarding the governance of the licensed entity. The qualifications required should include legal, investment, risk and company management, accounting, compliance, etc.

Directors can be categorized as: executive or non-executive and interested or independent. Interested directors are employees of the fund's investment manager and should be considered as conflicted. Independent directors do not have any significant relationship with the fund's managers but shouldn't have

either any relationship with the fund's service providers so as to avoid any potential conflicts of interest. Other conflicts of interest can arise when a director is sitting on the board of two funds with different investment managers but substantially the same investment strategy or when a director sits on a number of other funds promoted by the same manager (and derive substantial income from this relationship with the manager). Executive directors are full-time employees involved in the day-to-day management of the company. Non-executive directors have a part-time and intermittent involvement with the company. It is, however, worth noting that non-executive directors have the same legal duties, responsibilities and potential liabilities as their executive counterparts.

The salary of the board members is a good indication of what should be expected from the directors. A standard level of remuneration for directors is approximately 3'500 (USD) per year (i.e. 7hrs at an hourly rate of 500/hr). The director in that case will devote less than two hours every quarter to his task. This level of remuneration express the fact that the investment manager is not expecting a significant contribution from the director and its acceptance by the directors is also a recognition that he will not have to devote too much time and mind to the job. Directors' remuneration is

usually disclosed in the fund's offering memorandum or can be found in the annual financial reports.

Directors should acknowledge that while they will outsource part of their duties to third parties the responsibilities remain those of the board. Directors should therefore not only monitor very closely not only the investment manager, but also all the other service providers, and ensure that those entities recognize the fund and not the investment manager as their client.

According to a recent article in the Alpha magazine, the pool of willing directors is actually quite finite and small says Steven Whittaker, a lawyer at London-based Simmons & Simmons and author of a how-to-be-a-director guide for the London-based Alternative Investment Management. As the hedge fund industry booms, the law of supply and demand drives up directors' fees. People have identify this opportunity and serve on the board of several funds for a living. Some have even organized themselves as a service provider company where the service is proposed as a commodity.

Investors should be very attentive to the quality of the board of directors before investing in a fund as directors are in the best position to protect their interest.

Wood River - Has anyone done a due diligence?

Lehman Brothers sued Wood River Capital Management, a hedge fund that claimed to have a diversified investment style in October 2005. The fund owed Lehman \$20 million.

In October of 2005, the SEC began its investigation into Wood River Capital Management and John H. Whittier, the investment manager. The actions stemmed from two frauds that took place within the fund.

First, 65% of the fund's assets were invested in a small technology company called EndWave. This is vastly different that the 10% cap on long positions as written in the fund's offering memorandum. Second, the fund listed their auditor as American Express Tax & Business Services Inc. and their administrator as NAV Consulting. Both these companies deny any form of business relationship with Wood River. The scam resulted in investors losing \$88 million.

Other warning signs to investors were that in 2002, the landlord of its San Francisco office sued the company for non-payment of rent. The second is that the fund's executives had never presented audited financial statements.

Whittier was sentenced to 3 years in prison and a fine of \$5.5 million. Most recently, on July 29, 2008, a New York State court Judge, Charles Ramos, ruled in favor of UBS in a lawsuit filed by Wood River investors. The investors claim that UBS, knowing Wood River's position in EndWave, shorted the stock to profit over \$100 million. Ramos said, "the facts alleged do not support the causes of action ... these plaintiffs lack standing"



Hedge Fund Blow-Up Meter

Funds added:
WexTrust Capital
Number of Funds
1
Total Loss (\$ml):
100
(started July 2008)

Latest Additions to our Library

- Glenrock Global Partners (BVI) Inc.
- Karsch Capital Ltd.
- Lafayette Street Fund Offshore, Ltd.
- M. Kingdon Offshore Ltd.
- Pequot Core Global Offshore Fund, Inc.

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