LESSONS FOR NEW EMERGING FUNDS

NICK TSAFOS, **MIKE LAVEMAN** AND **JEFF PARKER** LOOK AT BEST PRACTICES FOR FORMING A FUND AND EXPLAIN HOW **EISNERAMPER** CAN HELP WITH THE PROCESS

Nicholas Tsafos
is an audit partner with 25 years of diversified accounting and auditing experience. His practice is primarily devoted to hedge funds, private equity funds, broker-dealers in securities, registered investment companies and investment advisers.

Michael Laveman
is a tax partner and member of the Financial Services Group. He is involved in the structuring of investment funds and related entities, as well as in providing advice on the tax complexities of financial products and investment strategies.

Launching a hedge fund can be a daunting and complicated process, with various factors to take into consideration and pitfalls to avoid along the way. EisnerAmper provides services to managers forming new funds and helps them incorporate best practices and standards. *HFMWeek* caught up with partners Nick Tsafos, Mike Laveman and Jeff Parker to find out more.

HFMWeek (HFM): What are the key considerations for hedge fund managers starting up in the US?
Nick Tsafos (NT): Most important is regulation. Fund managers in the US need to understand the regulations around hedge funds here, for example the '33 Act, '34 Act, '40 Act, Dodd-Frank, and JOBS Act. When you're devising a strategy for a hedge fund you need to keep these all in mind because regulation has control over all the operations. In addition, the regulations are ever-changing – and growing.

What's even more important in terms of raising capital is having a business plan. A lot of advisers who start a fund think that if they just talk about their strategy, investors will want to invest. That doesn't happen anymore. It's very important to develop a business plan that talks about your business strategy, how you're going to execute that strategy to achieve the rates of return that you hope to achieve, and the capital levels to which you want to grow. By putting everything down on paper, you're making and documenting decisions about the type of service providers you're going to need, the type of infrastructure you're going to build to meet the regulatory requirements, and the needs of investors.

Investors also want to see that you're capable of executing the business plan you present. It's very important that you can persuade your investors to buy into what you're doing and that you'll be able to do it. These elements will set you apart from other investment advisers.

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HFM: What key pitfalls should a new manager avoid?
Mike Laveman (ML): These days you need to have realistic timing expectations of getting a fund off the ground. It probably takes two or three times longer to get a fund up and running today than it did five years ago because of the challenging fund raising environment. Managers should make sure they have enough start-up capital to get them through this period.

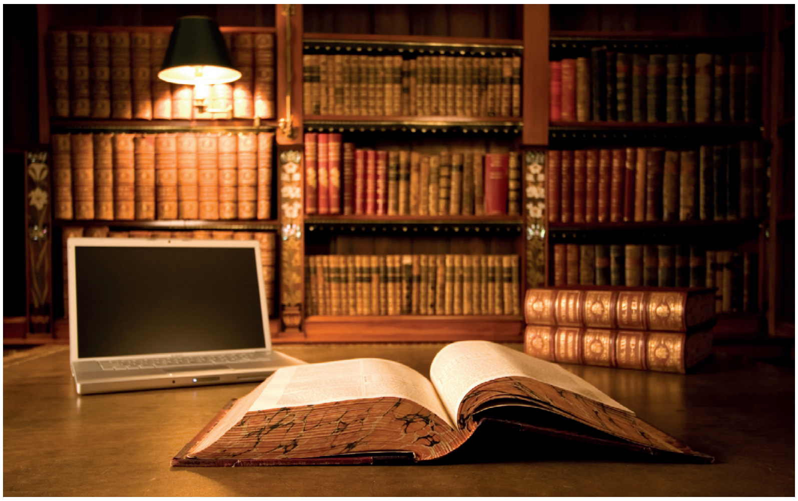
Building an infrastructure that can grow as the fund grows in complexity and size is very important. Many fund managers focus on the near-term, but also need to spend time thinking ahead to what challenges they will face in the future. Having flexibility in the fund documents is a critical part of this. It is also important for fund managers not to neglect allocating time related to setting up their management companies and incentive fee vehicles as well as considering employee compensation issues.

Finally, making sure that you're working with the right service providers, with the right experience and expertise who can grow with your business is very important.

HFM: How can EisnerAmper help new hedge fund firms during the start-up stage?
ML: We've been working with hedge fund managers for more than 30 years, many of which are (or started with us when they were) emerging managers. We have a high level of partner involvement from day one. We deal with all the practical implications of starting up a new business. A lot of start-up managers don't have a business plan or the expertise of running a business so we spend a significant amount of time on the structuring issues, types of entity to set up etc. It's something that we've really excelled at for many years.

We can also provide business advice on insurance needs, assist with IT/space consulting, provide outsourced CFO services, and make introductions to resources which may be able to help the manager grow. Tax planning for the manager, especially in the estate tax area, is also a very important topic we discuss.

One particular service that we are seeing a demand for, particularly from smaller managers, is for us to review past performance returns. Typically referred to as agreed-upon procedures, these attestation services can provide potential investors additional comfort from the returns the managers are touting in their marketing materials.



NT: Our clients consistently rank us very high for client service. We're always willing to talk about and share our knowledge.

Jeff Parker (JP): One thing that we always stress internally to our employees and partners is that the investors in the funds are the fund managers' clients. Whether it's timing of deliverables or expertise, we really pride ourselves in advising fund managers for the benefit of their investors.

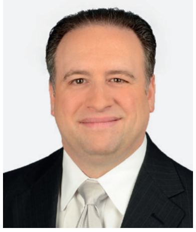
HFM: How does EisnerAmper's service stand out or differ from the competition?
JP: One way in which we stand out is with our size. We are large enough to have the right amount of expertise but small enough to still be able to provide great service. With regard to our fund practice in general, a significant portion of our client base is funds.

At the same time, we have substantial experience in what I would call ancillary services, such as valuations, international planning, state local planning and personal tax services, etc. Many of our clients see value in taking advantage of these as well – and appreciate the comprehensive perspective it allows us to bring to their ventures. We often find that our clients may have a relationship with a smaller accountant who has been handling their personal work for years, but they quickly realise that they have outgrown them and need personal income tax preparers that really understand the fund world.

Another thing that makes us different from our competitors is that we've got a very high degree of partner involvement, from the initial proposal stage to servicing our clients. Some of our competitors may bring in top-level people for the initial meeting, but they do not get involved in the details of the engagement.

NT: What's also of value are our offices in the Cayman Islands and India, which provide us an international perspective and presence. We have the kind of expertise not typically expected of firms our size.

JP: We also provide a lot of education for our clients through webinars, events and publications to keep them current and advise them on a host of issues relevant to their ventures.



Jeffrey S. Parker,
CPA, MBA, MST, JD, is a tax partner specialising in advising investment partnerships, funds of funds and broker-dealers, including structuring and compliance. Jeff also advises fund managers on personal tax returns and planning.

HFM: What factors do new fund managers need to consider from a tax perspective?
JP: Within a fund's strategy there are certain tax ramifications, such as whether the fund is classified as a trader or an investor. This has a large tax effect on the ability to take deductions. By better understanding the rules and their implications, managers can structure their funds to support their strategies with optimum tax efficiency.

Certainly doing business in New York City is significant from a marketing perspective but it is also very expensive. Managers need to understand the pros and cons and whether it makes sense to incur the tax costs to be in New York. Structuring of management companies has other effects as well, such as self-employment tax and the new net investment income tax, also known as the Obamacare tax.

Another area that's also become very important from a tax perspective is Fatca. Fortunately we have a lot of expertise in this area; Mike Laveman is one of the co-leaders of our Fatca initiative. The structuring and much of the registration obligations need to be happening right now, so funds need to make sure they have the flexibility and understand what they need to do under Fatca.

HFM: What standards do fund managers need to meet to ensure best practice?
NT: Investment advisers have to be able to show that they can meet all the regulatory requirements and provide information to investors. They need to have a good understanding of the business environment that they're in and be able to showcase that understanding when they're speaking to investors. We ensure they not only do it right – but can aptly discuss the issues and nuances.

The managers also need to ensure that they understand the investors' needs and how those needs fit into their investment strategies as well as the operational infrastructure. Because of our experience advising clients with an eye towards their investors, we can provide insight to those needs.

Managers also need to have an infrastructure that gives them a platform to support many investment vehicles, not just hedge funds. Whatever the case may be, investment advisers need to understand the business environment, the implication of their structure and options, and be able to discuss them in a manner that impresses investors. ■

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