

US

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And along came Bernie

In the US, the battle over the regulation of hedge funds has been gaining intensity for some time. Congress has been discussing regulation of the industry for over two years. On November 10 2008, Senator Charles Schumer told a securities industry group that he thought it was time for a single US regulator to be given responsibility for the regulation and oversight of private capital firms, including hedge funds. On November 13 2008, the House Committee on Oversight and Government Reform heard testimony from five leading US hedge fund managers. Committee chairman Henry Waxman began by observing that, with assets exceeding \$2 trillion, hedge funds have the potential to constitute a systemic threat to the global economy. He referenced several concerns including excessive leverage, the lack of transparency and the disproportionately favourable tax treatment accorded to hedge fund earnings. The hedge fund managers offered statements defending their industry, their personal wealth, the capital gains tax treatment and the need for confidentiality. One manager indicated that he could see the need for some limitation on leverage. The managers all made the point that excessive US regulation would exacerbate the trend towards concentrating hedge fund activity and related jobs outside the US.

It was obvious that the battle lines were forming and acquiring definition. All in all, it looked like the sides were fairly evenly matched. And then, in mid-December, along came Bernie. Everything has changed. Bernard L Madoff, one of the most prominent US hedge fund managers, was arrested in New York on December 10 2008 and accused of perpetrating a \$50 billion fraud. He has apparently admitted to orchestrating the largest Ponzi scheme in US history. His investors, who are sophisticated, influential and global, appear to have lost most, if not all, of their investments in his fund. As a registered investment adviser, the SEC could have examined Madoff's fund at any time during the last three years, but it appears not to have done so. Whether or not justified, the

SEC will be criticised by Congress for this oversight. At a time when the hedge fund industry is suffering its worst year (and highest redemptions) on record and is already under intense pressure to accede to regulation, Madoff may turn out to have been the decisive factor. He has resolved, perhaps single-handedly, the question of whether there will be comprehensive hedge fund regulation in the US.