Funding the Future

Offshore hedging increases risk

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Interesting to note that the FT reports the following this morning:

Man Group's US brokerage has told a US court that a subsidiary of UBS, the Swiss bank, was partly to blame for failing to spot an alleged $179m (£90m) fraud at a Philadelphia hedge fund.

The Cayman Islands administration business of UBS was added last Friday as a third-party defendant to a case being brought against Man Financial by the hedge fund's receiver.

In essence this is a case about people abusing trust to commit an alleged fraud. As the FT summarises it:

The case involves the hiding of $179m of PAAM trading losses in a sub-account at Man. Clark Hodgson, the receiver, has accused Man and several of its employees led by Thomas Gilmartin, a senior vice-president, of colluding with PAAM to conceal the losses and shift the date of trades.

But let's be clear. The hedge fund claimed to be in Philadelphia but was operated on contract in Cayman. And UBS might be Swiss but a front company of theirs supposedly did the work on a beach in the middle of the ocean. If you will trust serious funds to such a dubious arrangement, in a location where the underlying ethos is to beat the system, what form of contributory negligence are you guilty of?

And, more importantly, to what sort of risk does this sort of offshore hedging expose the whole financial community? Too much, you can bet, for it to survive a meltdown without serious consequence for real people doing real jobs to create real wealth. None of which are things with which hedge funds are well acquainted.