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Lawsuit Points Out Unusual Fee Use

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A brokerage firm may have used management fees it collects for running multi-manager hedge fund vehicles to pay unrelated legal expenses — a practice that might raise eyebrows among those entities' shareholders.

The alleged payments came to light in a lawsuit that **Richard Roth** of the **Roth Law Firm** in New York filed against Steven and Martin Sands, who run a brokerage that's now called Laidlaw & Co. **Roth** claims the outfit, formerly known as Sands Brothers, owes him legal fees, primarily for defending it against claims by clients who had come forth with accusations of over-aggressive and unauthorized trading and mishandling of accounts from 1993 to 2003.

He's suing for more than $1.5 million, to get back what he claims he is owed plus interest.

The possible issue for fund investors: **Roth's** July 11 complaint, lodged in New York State Supreme Court, includes an exhibit in which he claims the Sands brothers had paid him in the past, but never out of their own pockets. Rather, the checks came from a number of their New York firm's investment vehicles, including five funds of funds operating under the Select Access banner.

Payments also came from what appears to be a venture capital vehicle and Amerindo Technology, a mutual fund run by the unaffiliated Amerindo Investment. In all, the checks added up to $25,000 to $30,000, according to **Roth's** complaint.

Roth added in the complaint that when he asked Steven Sands why the payments were coming from entities unrelated to the cases he was working on, Sands regularly replied, "It's my money," or "the funds are coming out of my management fees."

While lawful, using management fees for such matters does raise questions about a fund operator's obligations to its clients. On the one hand, it wouldn't hurt a fund's performance to pay unconnected legal fees with income from management charges, which are usually equal to 1% of assets for a fund of funds. On the other hand, there's an expectation that managers are plowing that income back into resources that benefit their vehicles, such as research and staff salaries — while using performance fees as they wish.

Still, the implication for the Select Access vehicles' investors isn't entirely clear.

The Sands brothers, meanwhile, have filed a motion to seal court documents from the public.

Their firm's Select Access vehicles have performed a bit worse than Hedgefund.net's fund-of-funds index, which was up 6.6% for the first five months of this year. The first Select Access vehicle, with $28.5 million under management, gained 4.9% over the same timeframe. Select Access Institutional, with $30.3 million, netted 4.5%. The $20.4 million Select Access 3 posted a 6% return. ♦