

## FUND GOVERNANCE

# Former General Counsel and Current Independent Director Discusses the Importance of Robust Fund Governance

By Michael Washburn

William H. Woolverton recently joined the New York office of DMS Governance Ltd. (DMS) as managing director and head of U.S. legal. In this role, Woolverton has oversight of U.S. legal for DMS, along with senior responsibilities relating to DMS' U.S. business, and serves as an independent director on the boards of investment funds and related structures. Prior to joining DMS, Woolverton was senior managing director and general counsel at Gottex Fund Management, where he was responsible for managing fund administration and governance of all onshore and offshore funds and oversaw the management of external legal relationships. Previously, Woolverton spent over 15 years at Putnam Investments where he managed a staff of more than 100 legal and compliance professionals, and before that he was a senior lawyer at Alliance Capital Management Corporation.

The Hedge Fund Law Report recently interviewed Woolverton in connection with his move to DMS, during which he discussed the role of robust fund governance in the context of private funds.

For additional insight from Woolverton, see "*ALM General Counsel Summit Reveals How Hedge Fund Managers Can Adopt a Robust Compliance Program and Address FCPA Risks*" (Dec. 3, 2015); "*What Should Hedge Fund Investors Be Looking for in the Course of Operational Due Diligence and How Can They Find It?*" (Oct. 13, 2011); and "*Fifth Annual Hedge Fund General Counsel Summit Covers Insider Trading, Expert Networks, Whistleblowers, Exit Interviews, Due Diligence, Examinations, Pay to Play and More*" (Sep. 22, 2011).

For commentary from DMS' founder, see "*Don Seymour Discusses Hedge Fund Governance and the Impact of the SEC-CIMA Cooperation Arrangement on Hedge Fund Manager Examinations*" (Apr. 5, 2012).

**HFLR:** *What motivated your move to DMS, and why is it happening at this particular stage of your career?*

**Woolverton:** I joined DMS for several reasons. The first is that I really believe in the importance of robust fund governance for private funds and also of course for public funds. For many years, I have seen DMS take responsible fund governance very seriously. The other reasons I joined DMS include the rigorous training DMS provides to its employees so they will be effective fund directors, as well as the firm's technology platform that enhances the directors' abilities to focus on the key issues associated with fund governance.

In addition, I have been very impressed with how DMS has built a first-rate management company for Undertakings for Collective Investments in Transferable Securities (UCITS) and alternative investment fund manager offerings in each of Luxembourg and Ireland, primarily working with U.S. managers. In my career, I have structured many funds in both jurisdictions, so in my role with DMS, I will also get the chance to work on European product innovation and strategy, which is very appealing to me.

[See "*Post-Brexit Cross-Border Marketing Options and the Viability of Domiciling Funds in Luxembourg (Part One of Two)*" (Nov. 10, 2016); and "*Domiciling Funds in Germany or Ireland to Access the E.U. Post-Brexit, the Possible Introduction of PRIIPs and the Rising Prominence of UCITS Structures (Part Two of Two)*" (Nov. 17, 2016).]

As to why I've transitioned at this stage of my career, fund governance is personally very important to me. I arrived at the view that, in this new role, I can have a far more meaningful impact on fund governance by serving as an advocate for strong fund governance policy and articulating what it really means to be doing things

the correct way as a fund director. I can do all of these things more effectively at a firm like DMS as opposed to being a general counsel or an attorney in a law firm, where fund governance would not necessarily be the primary focus of what I would be doing. This will really be the mission for the rest of my career.

***HFLR: An independent director plays a role that perhaps might not be in such wide demand if regulations were clear and consistently enforced. Do you believe that fund managers and investment advisers receive sufficient guidance from the regulators?***

**Woolverton:** If you think about the governance structure for publicly registered mutual funds in the U.S., or for that matter UCITS structures in Europe, there is a well-established set of expectations and indeed requirements for directors and trustees of publicly registered funds. Here in the U.S., they are set out in the Investment Company Act of 1940 (Investment Company Act). As a result, advisers don't have to spend a lot of time figuring out how to do things. Congress tells them in the form of the Investment Company Act, and the SEC promulgates rules under that act. Basically, the road map is very clear, and it's enforced by the SEC.

For private funds established in various offshore jurisdictions, the guideposts are perhaps less rigid than can be found under the Investment Company Act. This is the reason that private funds need strong governance and independent directors who are highly qualified to do their jobs.

Over the past 5 to 10 years, a trend has developed with larger institutions investing in private funds, whether hedge, private equity or venture capital funds. This trend reflects a shift in the demographics of private funds as compared to 15 or 20 years ago. Many institutional investors – who themselves represent people like teachers, police, firemen and pensioners – have been keenly focused on the importance of robust independent fund governance. [See “*Dechert Global Alternative Funds Symposium Evaluates Liquid Alternative Funds and Fund Governance Trends*” (Jun. 25, 2015).]

What I've seen for years is that, if an investment manager or sponsor of a hedge fund wants to raise capital, it has become more important for them to be able to say to investors, “I've got thoughtful directors, and a majority are independent.” [See “*SEC Chair Outlines Expectations for Fund Directors*” (Apr. 7, 2016); and “*PwC Benchmarks Alternative Asset Manager Governance Practices*” (Oct. 5, 2015).]

The independence factor is important, and in a sense, it follows the framework of publicly registered funds in the U.S., where mutual funds are required to have a majority of independent directors. Institutional investors expect that the private funds that they invest in will have a board where a majority of the directors are independent from the investment manager.

***HFLR: Do you find that regulations complicate or impede cross-border fund transactions to a greater extent than previously?***

**Woolverton:** From the perspective of new regulation, I think there are a few things that have happened that create hurdles to fund launches, but I don't think they're insurmountable hurdles. For example, there are new compliance requirements that fund managers must be aware of, such as FATCA, and, if they are in Europe, the Alternative Investment Fund Managers Directive.

[See “*Six Challenges in Connection With FATCA Compliance by Hedge Fund Managers*” (Mar. 13, 2014); and our series “*Steps That Alternative Investment Fund Managers Need to Take Today to Comply With the Global Trend Toward Tax Transparency*”: Part One (Apr. 7, 2016); and Part Two (Apr. 14, 2016).]

***HFLR: Are your clients particularly attuned or sensitive to any recent rulings at the regulatory level?***

**Woolverton:** The whole subject of liquidity in private funds is, of course, a hot topic going back to 2008 when liquidity disappeared, hedge funds gated and there were many unhappy investors. If you follow the history of the regulatory consideration of the liquidity issue over the past ten years, however,

it has culminated in the SEC's issuance of Rule 22e-4 under the Investment Company Act, which imposes liquidity requirements and constraints on mutual funds and ETFs.

[See "*FSB Recommends Essential Risk Mitigation Requirements for Asset Managers*" (Aug. 25, 2016); "*Focus on Hedge Fund Managers and Market Liquidity May Be Overemphasized, Argues FCA Director*" (Mar. 31, 2016); and "*FCA Expects Hedge Fund Managers to Focus on Liquidity Risk*" (Mar. 3, 2016).]

Hedge fund managers that are based in the U.S. and registered with the SEC under the Investment Advisers Act of 1940 need to consider whether the SEC could begin to think about imposing liquidity constraints on their hedge funds to prevent the gating issues we had in 2008 and 2009. Historically, the SEC has focused on protecting mutual fund investors. When it comes to private funds, they are less present because it is harder to invest in hedge funds. However, because the SEC is so focused on liquidity, and protecting liquidity in fund investments, it forces hedge fund managers themselves to think about liquidity issues more than in the past.

**HFLR:** *Have the approaches or attitudes of fund managers changed along with the shifts in the regulatory environment?*

**Woolverton:** I think that fund managers and sponsors are more attuned these days to the importance of launching funds that are really going to do what they say they are going to do and deliver the level of investment performance that is promised. This change extends, primarily, from 2008 and 2009. Prior to the 2008 global financial crisis, some fund sponsors may have been less rigorous in their back-testing analysis.

Does that mean it takes longer to get a fund to market than it used to? Perhaps. In the end, you're left with funds that are more successful with fewer surprises for investors, and I think that's a good thing.

Managers have developed the frame of mind and the skills to be more protective of their own investors. All of that ties back to certain duties that fund managers and directors have to their funds that are grounded in common law concepts such as duty of care and basic fiduciary principles. [See "*What Are the Duties of Directors of Cayman Islands Hedge Funds, and Should Those Duties Be Codified?*" (Feb. 13, 2014).]

**HFLR:** *What trends do you foresee with respect to hedge fund strategies and styles?*

**Woolverton:** As the equity markets perform well, what you're going to see is that there are more hedge funds that are oriented toward equity investment, such as long-short hedge funds. As the equity markets go through downward cycles, what you'll be seeing are hedge funds that are not correlated to equity markets. You could see real estate funds, real asset funds or infrastructure funds, all making investments that are not necessarily correlated to the performance of capital markets themselves.

At least currently, the long-short hedge fund area is reasonably robust and credit strategies are doing reasonably well. Those trends change constantly, however, making it hard to generalize.