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Hedge Fund Managers Claiming Bailouts as Small Businesses

By Katherine Burton and Joshua Fineman
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- Loans are part of the $2 trillion package to prop up economy
- Consultant warns that seeking aid shows ‘poor moral judgment’

Pedestrians walk past the New York Stock Exchange on a nearly empty Wall Street in the Financial District of New York. *Photographer: Gabby Jones/Bloomberg*

Free money.

That’s the enticing prospect hedge funds and other trading firms are pondering after realizing they too might be able to participate in a historic U.S. stimulus package to keep small businesses alive through the coronavirus pandemic.

Since early April, law firms have hosted Webinars and sent out alerts, and accounting firms have reached out to clients, all with the goal of explaining how they might be able to tap into the Paycheck Protection Program. The $349 billion package administered by the Small Business Administration provides loans to cover payroll, rent and utilities for up to eight weeks. The loans can convert to grants if recipients retain or rehire their workers.

Some hedge funds already have applied, filling out forms to show they have fewer than 500 employees and certifying the “current economic uncertainty makes this loan request necessary to support the ongoing operations.”

Ironically, hedge funds are designed to employ as few people as possible so star traders don't have to share millions of dollars in fees. The industry gets its name from the premise it can generate gains even when markets fall.

The question of whether to partake in the program is dividing members of the money management community. Some traders have called it morally corrupt, while others insist they are small businesses -- just like hair salons, restaurants and dry cleaners -- that could use a helping hand after global markets tumbled and cost them money. Given that the program is first come, first served, some managers were quick to submit their paperwork, according to market participants, even if eligibility remains unclear.

Donald Motschwiller, head of First New York, a trading firm that runs $2.9 billion in assets, said he was still deciding whether to request money that could be used to pay employees, including a receptionist and office manager, who are still on the payroll even though, with everyone at home, they essentially don't have jobs to do. He canvassed about 15 hedge funds in his circle, from small managers to multibillion-dollar firms, "and no one has said 'no'" to the possibility of taking the loan, he said.

Scaramucci's Defense

The industry's most prominent firms probably have no interest in the program, but it might make sense for money managers to apply if they are just starting their businesses and gathering capital, said Anthony Scaramucci, owner of SkyBridge, a firm that farms money out to hedge funds.

"Just because the business has a name, private equity or hedge fund manager, doesn't necessarily mean that they're loaded with rich people," he told MSNBC in an interview earlier this month. Some are in their 20s and scared, he said.

The chatter among money managers has grown loud enough to prompt a warning last week from Aksia, which advises institutional investors on placing money with hedge funds and other alternative investment firms. The firm said it would view any opportunistic use of the program "negatively" when counseling pension funds and other institutions with about $160 billion to invest.

A manager with a healthy business who takes advantage of a program that isn't "precisely defined, is not only showing poor moral judgment and potentially hurting the reputation of the alternatives industry, but it's also probably crowding out struggling workers and businesses severely impacted by Covid-19," Aksia said in the memo.

'Complete Abomination'

Some lawyers have cautioned their clients that they may yet be disqualified. While the rules make clear that banks and insurance companies aren't eligible for the small-business loans, the guidelines are murkier regarding hedge funds and proprietary trading shops. The Treasury and the Small Business Administration could yet come out with clearer policies that prevent those firms from participating. Representatives for those departments either didn't immediately respond to messages or had no immediate comment.

One manager, who asked not to be named, said he was outraged when he received a note from his accountant analyzing his potential eligibility. Why, he asked, would a hedge fund that collects management fees, and can make money if it's skilled, avail itself of a government handout?

"It's a complete abomination," agreed Nate Koppikar, a partner at San Francisco-based money manager Orso Partners. He noted that firms that avail themselves of the money may later be publicly identified under the Freedom of Information Act.

A spokesman for former Vice President Joe Biden, the expected Democrat presidential nominee, shared similar sentiment.

"Leave it to the Trump administration to execute a program meant for America's small businesses in a way that instead gives relief to hedge fund managers who don't need it -- while mom and pop shops are forced to wait in line," spokesman Andrew Bates said in a statement. "The Trump administration has shown its hand: their priority is to take care of the wealthy and well-connected as fast as possible and with as few conditions as possible."

The Managed Funds Association, the hedge fund industry group, also came out against using the loans, though somewhat less stridently.

"While we recognize that every manager must make their own decision about the viability of their firm, we have provided guidance to our members that we do not believe the money in this program was intended for managers general partnership interests," Bryan Corbett, president and chief executive of the organization, said in a statement.