

Financial Institutions

Loss Scenarios

Hedge Fund Market Manipulation Results in Litigation

Cause of Action: Securities Violation, Fraud

Type of Organization: Hedge Fund



Description of Event:

The Japanese Securities Exchange Commission investigated a Hong Kong based hedge fund's directors and officers, alleging that they were involved in short selling and fraud aimed at manipulating the value of stocks. The Japanese securities commission concluded its investigation and found no wrongdoing. Subsequently, the Securities and Futures Commission (SFC) in Hong Kong began an investigation into the same hedge fund's Chinese operations, alleging the same wrongful conduct. Following a three year investigation, the SFC issued a formal notice of charges for securities violations against ten directors at the hedge fund. The hedge fund retained separate defense attorneys for the individuals being criminally charged.

Resolution:

The insured settled the lawsuit with the SFC for the equivalent of a \$50,000 penalty and a revocation of licenses. Although no monetary damages were sought, the insured incurred defense costs of more than \$1,500,000. Because the hedge fund had a local professional liability policy, the definition of insured person was significantly broader and included individuals working in an insured capacity, as such defense costs coverage was provided for all ten individuals. Because the master professional liability policy had a DIC/DIL endorsement, the master followed form to the local policy and provided 100% defense cost coverage. If the hedge fund did not have a local policy, only 40% of defense costs would have been covered under their master policy's allocation provision.

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