

Hedge Hell

Investors who were attracted to Highland Capital's tough investment style are now feeling a little roughed up.

By Nathan Vardi

BEFORE THE CREDIT CRISIS hit, investors poured money into hedge funds run by Highland Capital Management in Dallas, which at its peak was running \$38 billion. The two founders, James Dondero and Mark Okada, had a reputation for scoring big returns using leverage and tough tactics like squeezing fees out of companies whose outstanding debt Highland purchased. Now three of Highland's funds, including its Crusader Fund, have failed, and investors are getting more of Highland's hardball tactics than they bargained for.

The investment firm handling money for Brazilian billionaire Moise Safra has been trying to extract its \$13 million investment in the crashed Highland Credit Strategies Fund for over a year. Highland accepted its redemption request early in 2008, saying it would return the cash in stages. But Highland forked over only \$400,000 before telling investors in October that the hedge fund was going out of business and would distribute what little was left pro rata.

Safra's firm sued Highland for breach of contract in November, and in February Highland seemed to relent, floating a plan that would see 85% of the fund's assets distrib-



uted first to those who redeemed prior to October 2008. That would help Safra but not leave much for others, as Credit Strategies is down substantially and had only \$230 million or so in assets left as of December, court documents say.

One of the investors that would be cut out is 3A Alternative Funds, a Swiss fund of funds. It claims in a suit filed in April that Highland concealed the fund's troubles by not revealing hundreds of millions of dollars in redemptions in the months prior to the fund's implosion. 3A says it didn't submit a redemption request as a result. A mediator will try to sort things out.

Another investor, the British bank Barclays, says it exercised its special right to immediately redeem from the funds in October 2008 but that Highland refused. Highland's response? Barclays did not take the necessary steps for redemption.

Complicating the workouts is Highland Capital's big investment in its own funds. In the past Highland Capital, which is owned by its employees, boasted that this aligned its interests with those of investors. But investors like Safra say the insider ownership could "wrongly benefit Highland" when distributing any money.

Says Highland in a statement: "It was in its investors' best interests to conduct an orderly wind-down of the funds." **F**