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Madoff Investors Paid Fees to Funds for Profits That Vanished

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Jan. 9 (Bloomberg) -- Investors wondering what happened to the $50 billion that disappeared in Bernard Madoff's alleged Ponzi scheme need look no further than the fees charged by the hedge funds that marketed his money-making prowess.

Many investors left their savings in the Madoff-run funds, content in the belief that their nest eggs were doubling every seven years. Firms that sold the feeder funds, including Fairfield Greenwich Group, Tremont Group Holdings Inc. and Bank Medici AG, were paid fees every year.

"The people who put money into those feeder funds generally let their investments ride," said Ross Intelisano, a lawyer at New York-based Rich & Intelisano LLP retained by clients who had more than $100 million with Madoff.

The eight largest Madoff-only vehicles had a combined $27 billion in assets. That's more than half of what the 70- year-old financier, who was arrested on Dec. 11 in New York, said was lost in the scheme. Their role in the scandal has damaged the reputation of funds of funds, which tout their ability to select superior investment managers, and exposed them to client lawsuits.

Fairfield Greenwich's Fairfield Sentry fund had about $2.7 billion in its Madoff funds in 2000. Assuming that no additional cash was invested or redeemed after that time, the New York-based firm would have taken out about $450 million in the next eight years, its 20 percent cut of investment profits. That doesn't include an additional fee equal to 1 percent of assets that the firm, co-founded by Walter Noel, initiated in October 2004.

Wiped Out

Based on Madoff's reported returns and a 20 percent performance fee, principal invested at the end of 1990 in a feeder fund would have been completely wiped out by 2005, assuming that Madoff didn't do any investing in that period.

The firm should return at least $1 billion in fees it wrongfully accepted from investors, according to a proposed class-action, or group, lawsuit filed yesterday in Manhattan federal court by Los

Angeles-based Pacific West Health Medical Center Inc. Employees Retirement Trust. Fairfield Greenwich had $7.5 billion with Madoff as of last month.

“The fees were inappropriately paid because they were based on assets and performance that didn’t exist,” the trust’s lawyer, Robert Finkel of the firm Wolf Popper in New York, said in a phone interview. “They didn’t actually earn that money and they’re obligated to return it to investors.”

“The company did indeed perform extensive due diligence,” said Thomas Mulligan, a Fairfield Greenwich spokesman.

Fees Vary

Investors with Tremont Group Holdings and Ezra Merkin’s Ascot Partners LP have also gone to court to recover their money. The U.S. Securities and Exchange Commission is looking into whether hedge funds failed to conduct adequate due diligence on Madoff.

Representatives for Tremont, Ascot and Access all declined to comment. Representatives for Bank Medici and Kingate weren’t available to comment.

Feeder-fund fees vary. Some funds, such as Kingate Global Fund Ltd., charged 1.5 percent of assets a year, in addition to a 5 percent initial fee. London-based FIM Advisors LLP served as a consultant to Kingate. Other firms took a percentage of fund profits as well. Madoff said he got paid with commissions of as much as 3 percent on the stocks and options he traded.

Access International Advisors LLC, a New York-based firm that sold the LUXALPHA SICAV - American Selection fund, had about $720 million in assets at the end of 2004, according to Bloomberg data. Access International would have taken out about $80 million in fees during the next four years. The fund charged 0.8 percent of assets and 16 percent of the profits.

The amounts for the Sentry and LUXALPHA funds don’t include an initial one-time sales fee of 5 percent.

Checks Found

Thierry Magon de La Villehuchet, 65, who co-founded Access International, committed suicide in late December after the alleged Ponzi scheme came to light.

Investigators searching Madoff’s office after his arrest found about 100 signed checks, totaling about $173 million, ready to be sent to family, friends and employees, prosecutors said yesterday.

Officials previously disclosed that Madoff, before being apprehended, had told people he wanted to transfer $200 million to $300 million of his investors' money to "selected family, friends, and employees."

Investors in feeder funds with clauses that allow cases to be heard in arbitration are probably in a better position to get their money back than suits that are tried in court, said Intelisano, who brought cases against third-party advisers connected to Bayou Group LLC, a hedge fund that defrauded investors out of $400 million.

"Arbitration is cheaper, quicker and the cases are less likely to get thrown out," he said.

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