REUTERS

Bear Stearns likely to face hedge fund lawsuits

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By Martha Graybow

NEW YORK (Reuters) - Investors in two struggling Bear Stearns Cos. BSC.N hedge funds that made bad bets on risky mortgages will almost surely file lawsuits in hopes of recouping losses, but legal experts say they could have a tough time proving their case.

Already, some investors in the funds are talking to lawyers about bringing cases. Potential lawsuits likely would hinge on whether investors were fully informed of risks, lawyers say.

Ross Intelisano, an attorney who handles investor cases against financial firms, said his law firm has been contacted by two investors in the Bear Stearns funds -- a fund of funds and a small institutional investor he would not identify -- about possibly bringing lawsuits.

The law firm has not been retained in the Bear Stearns matter yet "but that may change," Intelisano said. His firm, Rich & Intelisano, currently represents investors who lost a combined $20 million in the 2005 collapse of the Bayou hedge fund amid charges of fraud and mismanagement.

The troubled Bear Stearns funds invested in complex portfolios of debt linked to the subprime-mortgage market, which has seen rising defaults. Bear Stearns has said it would lend $1.6 billion -- half of what it originally pledged -- to one of the funds to prevent it from collapsing. It said it does not expect to bail out the second ailing fund.

A Bear Stearns spokesman, Russell Sherman, declined to comment on Thursday when asked whether the Wall Street bank was aware of any lawsuits filed against it stemming from the hedge funds' problems.

Legal experts say that because hedge funds are aimed at sophisticated investors, including wealthy individuals and large institutions, it is hard for them to argue that risks were not properly defined or they did not understand them.

"If the disclosures were adequate, then it is a situation where the buyer has to beware," said Scott Tross, a litigation partner at law firm Herrick Feinstein. "It was all a question of how these funds were advertised to the people buying them."

Intelisano agreed that any potential case would likely depend on what was spelled out in the marketing materials and offering documents, which he said he has not seen, and that investors have a difficult time prevailing in these cases.

"Just because a hedge fund lost money, doesn't mean that there's a potential claim by an investor," he said.

The Bear Stearns situation is unique, said Ernest Patrikis, a partner at law firm Pillsbury Winthrop, because the Wall Street firm is injecting so much money into one of the funds in an effort to stabilize the situation.

Bear Stearns "really seems to be doing what it can to do the best out of a nasty situation," he said.

Lawsuits against hedge funds are a relatively new area, so any investor suits against Bear Stearns would be closely watched in the hedge fund world. More investors, such as pension funds and endowments, have added hedge funds to their portfolios in recent years.

In one pending lawsuit, the San Diego Employees Retirement Association sued Amaranth Advisors LLC in March for $150 million after the fund suffered $6 billion in losses -- the biggest hedge fund collapse ever. The investors contend that Amaranth violated its investment mandates by not diversifying its portfolio enough or guarding well enough against risk.

Amaranth, which last year had as much as $9.3 billion in assets, imploded last September after billions of dollars in bets in the natural gas market went sour.

In another case, investors in defunct hedge fund Wood River Partners have sued UBS AG (UBSN.VX: Quote, Profile, Research, Stock Buzz), contending that the Swiss bank earned profits by selling borrowed shares in the fund's biggest stock holding and helped other UBS clients do the same.

Wood River collapsed in late 2005, and its founder was charged by U.S. prosecutors earlier this year with defrauding investors out of $88 million.