

**An Open Letter to the
Hedge Fund Industry**

**Regarding
the Usage of Cash
Hurdles in Incentive Fee
Arrangements**

Dear Hedge Fund Industry Members,

We, the undersigned investors and consultants, advocate for the implementation of cash hurdles in incentive fee arrangements across the hedge fund industry. The long-term health of the industry is dependent on a healthy alignment of interests between GPs and LPs, and we believe incentive payments on true value-add fixes a misalignment that has been present in fee structures throughout the maturation of the hedge fund industry.

This misalignment has become increasingly evident in recent years, as risk-free rates have reached mid-single digits. A hedge fund may collect significant incentive fees based solely on skill-less returns generated from short rebate, securities lending, unencumbered cash, etc. These returns are easily obtainable by LPs outside of a hedge fund structure for free. Earning cash returns is not the reason institutional LPs invest in hedge funds.

Furthermore, cash hurdles better promote proper risk taking, as the financial health of the GP is dependent on delivering the valuable good LPs seek – alpha. In 2023, a \$1B market neutral hedge fund could have earned ~\$52MM (5.25%) returns just by holding cash, and if that fund charged a 20% incentive fee on absolute returns, would have taken home \$10.5MM in compensation for taking zero risk. This is not sustainable, especially as it seems the risk-free rate may remain elevated for the foreseeable future; and it is not what LPs are asking GPs to do.

We recognize that the implementation of cash hurdles means adjustments to fee schedules and operational procedures within funds. However, it is our firm belief that the long-term benefits of proper alignment vastly outweigh short term challenges.

Therefore, we urge the hedge fund industry to embrace better alignment and adopt cash hurdles in incentive fee arrangements as a best practice standard.

Signed,

continued

HEDGE FUND INVESTORS

BCV Asset Management	Pragma Gestão de Patrimônio LTDA
Bimcor Inc	Public Employees Retirement System of New Mexico
Brightwell Pensions	RBC Wealth Management
BW Gestão de Investimentos Ltda.	Sandstone Capital Pte. Ltd.
CDPQ	SECOR Asset Management
Credit Suisse Pension	Soros Fund Management
Employees Retirement System of Texas	South Carolina Retirement System Investment Commission
Fire & Police Pension Association of Colorado	Strategic Investment Management, LLC
Fondo de Ahorro de Panamá	Suva
FS Fiduciary Services LLC	Teacher Retirement System of Texas
GIC	Texas Permanent School Fund Corporation
Healthcare of Ontario Pension Plan Trust Fund	Texas Treasury Safekeeping Trust Company
Ilmarinen Mutual Pension Insurance Company	Trans-Canada Capital
Indiana Public Retirement System	TTC Pension Plan
John D. and Catherine T. MacArthur Foundation	UTIMCO (University of Texas/Texas A&M Investment Management Co.)
Kern County Employees' Retirement Association	University of Toronto Asset Management Corporation
Korea Investment Management	Utah Retirement Systems
LAB Ltd.	Utah School and Institutional Trust Funds Office
Los Angeles County Employees Retirement Association	Virginia Retirement System
Meketa Fiduciary Management	West Virginia Investment Management Board
New Mexico Educational Retirement Board	Wyoming Retirement System
North Dakota Department of Trust Lands	

continued

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