FORTUNE

Did Plainfield commit fraud? The FBI wants to know.

Posted by Katie Benner
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How one hedge fund went from being a high-flyer to being mired in a federal investigation for fraud.

Image via Wikipedia

The Federal Bureau of Investigation is probing whether Plainfield Asset Management, a hedge fund that once had $5 billion in assets under management, committed fraud by overstating the value of some of its investments and charging management fees based on those inflated assets.

Three sources tell *Fortune* they have been contacted by the FBI's Connecticut office with questions about Plainfield, including Stuart Meissner, a New York City lawyer who represents an anonymous whistleblower who made the same allegations in a civil complaint filed with the Securities & Exchange Commission on August 6. Meissner's client charges in his suit that Plainfield overvalued some investments so it could "defraud its own investors by unlawfully charging higher management fees than those which it is in fact entitled to." The complaint was filed under a provision of the recently enacted Dodd-Frank financial regulation law.

Meissner confirms that the federal investigation is ongoing. He says he "continues to receive calls from other people with significant information relating to the issues raised in the whistleblower submission. That information is from people with intimate knowledge of Plainfield. It has been passed on to the SEC and the FBI." Meissner adds that he is to meet with an FBI agent to discuss the matter in the coming days.

The government has been scrutinizing Plainfield since at least June, according to the people who have been contacted by investigators. An FBI spokesperson didn't return a call seeking comment.

Asked for comment, Plainfield provided a written statement: "This story is merely the latest iteration of a strategy of filing a baseless complaint with regulatory authorities against Plainfield, and then using the press to publicize the 'news' that the authorities are investigating the complaint. Our lawyers have advised us not to discuss this further at this time, but we want to be clear that the allegations against Plainfield are entirely without merit. We believe this reporter has shown a consistent bias against Plainfield in her reporting."

An exercise in judgment

In a letter to investors after news of the SEC suit was reported by the *New York Post* in August, Plainfield noted that "valuing a portfolio of assets that do not trade in the public markets is by definition an exercise in judgment." The letter stated that the SEC conducted a periodic exam of Plainfield in June 2009 that lasted nearly three weeks. "We had an exit interview with the SEC in October 2009, and no issue regarding valuation was raised," Plainfield asserted.

Plainfield was once a hedge fund on the rise, quickly growing from $150 million when it began in 2005 to nearly $5 billion at its peak in 2008. Plainfield co-founder Max Holmes was considered a distressed investing guru with a sterling track record from his days at DE Shaw. He is a popular adjunct professor at New York University's Stern School of Business who lectures on bankruptcy.

But, as *Fortune* chronicled earlier this year, the fund made a series of bad investments and was hammered during the financial crisis of 2008. Plainfield refused to let investors leave (which wasn't uncommon among hedge funds during the crisis), but continued charging those investors management fees (which *was* unusual). By early 2010, only 20% of the fund's assets consisted of money that investors actually wanted Plainfield to manage (and a chunk of that belonged to Plainfield employees). As of July, Plainfield's assets under management had dropped to $2.6 billion, according to *Absolute Return* magazine.

This is not Plainfield's first encounter with a criminal investigation. As *Fortune* reported this January, the Manhattan District Attorney is also investigating allegations that the firm engaged in a so-called loan-to-own scam. A handful of the fund's borrowers charge that Plainfield loaned them money, fabricated an event of default, and then took over their businesses under false pretenses. Plainfield has vehemently denied these allegations. Holmes has told investors that this case was created by borrowers who are conspiring to destroy his firm. The Manhattan D.A. declined to comment.

Plainfield has suffered the departures of key employees, beginning with the March departure of co-founder and head of corporate finance Niv Harizman. As reported by blogger Teri Buhl, Harizman left to start a fund called Tyto Capital Partners and took a managing director named Gregg Bresner with him. Founding partner and head of research Joseph Bencivenga also departed, as have senior vice president and corporate counsel Rayan Joshi, vice president of risk management Torjus Dalen, and partner and head of risk management James Daher.

The fund appears to be tightening its belt. In an effort to save money, Plainfield left its $7 million a year offices in Greenwich, Conn. and now operates from its disaster recovery site in Stamford.