

Lance Zinman Quoted on the Importance of Cybersecurity and IP Protection in the Quant Space

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Lance Zinman, Global Co-Chair of Katten's Financial Services practice, was quoted by *The Hedge Fund Law Report* in the third article of a three-part series on cybersecurity and intellectual property (IP) risks facing quantitative managers. Lance stated, "If you pick up a PPM for a quant manager, you will likely see more detail about certain risk factors. Those risk factors should go into detail about the importance and use of IP; threats to IP; the manager's dependence on systems; and what could happen if those systems experience interruptions or disruptions."

While quantitative managers are likely to have a good handle on cybersecurity by nature, protocols for handling a breach need to mirror those of fundamental managers. "Regardless of how a manager trades, cybersecurity is very important. Even if a cyber incident does not result in the disruption of a manager's trading systems (for example, a discretionary manager may be able to trade in a different manner), that manager will likely be subject to reputational harm."

Lance also noted that although IP is important to all traders, there are concerns specific to quantitative managers. "Quantitative algorithms are like the Coca-Cola formula, except the difference is that the formula for a quant manager changes every minute of every day. The code isn't developed and forgotten about; it is constantly being tweaked. Patent protection—as opposed to trade secret protection—is rare. Not only is it unclear whether these algorithms are entitled to patent protection, but if a patent is issued, the underlying invention is disclosed to the general public. Unsurprisingly, few managers want to disclose their algorithms." Managers also need to balance the needs of IP protection and investor due diligence. He added, "Investors generally engage in more technology, infrastructure, cybersecurity and business continuity diligence than they would for a fundamental manager. Quantitative strategies are based not only on mathematical formulas but also on the interconnection of those formulas with the technology and infrastructure the manager has in place."

Do not overlook using employment and confidentiality agreements as another tool for IP protection, as the statutory protection for trade secrets is limited and the costs of reproducing models are

relatively low. Lance stated, "As a general matter, these agreements, whether for a fundamental manager or a quantitative manager, will largely look the same and seek the same types of protection. But the IP provisions for a quantitative manager will be much more detailed and more clearly developed."

Lance noted that competition for talent is fierce despite growing interest in the field. "Quantitative managers are competing not only with Facebook and Google, but with other opportunities such as sports teams, which are increasingly employing analytics to evaluate players." ("An Introduction to Quantitative Investing: Special Risks and Considerations (Part Three of Three)," September 6, 2018)

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