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Group Wants Brokers To Divulge Omnibus Account Details

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WASHINGTON -- Brokers and others who sell mutual funds should be required to provide daily information to fund firms on shareholders who trade through so-called omnibus accounts, a lobbying group recommended in a newly issued study.

The Coalition of Mutual Fund Investors, a Washington lobbying group, said that without more information on omnibus accounts, mutual fund companies would find it "difficult or impossible" to curb abusive trading practices such as market timing.

Market timing, the rapid-fire buying and selling of fund shares, can be attacked with fees on shares that are redeemed quickly, the coalition said. The group endorsed a Securities and Exchange Commission plan for mandatory early-redemption fees, but said fund companies need more information to levy early-redemption fees on those trading through omnibus accounts.

A survey of 50 of the largest U.S. fund companies, which the coalition released Tuesday, found that nearly two-thirds already impose redemption fees on one or more domestic or international funds.

Fully 88% of the funds that charge redemption fees say they exclude, limit or waive redemption fees for those trading through retirement plans, brokerage accounts or other intermediaries, however.

Janus Capital states in the prospectus for its stock funds that its redemption fee "does not apply" to certain omnibus accounts, while American Century said its ability to monitor trading through such accounts is "severely limited," the study points out.

Omnibus accounts offer a single master account in place of numerous individual accounts. At the end of each trading day, brokers and other intermediaries typically net deposits and withdrawals into a single order placed with a mutual fund, shielding the identity of the individuals who are buying and selling. Critics say that allows abusive market timers to conduct trades without being detected and identified by fund companies.

"The study concludes that funds cannot effectively enforce their policies because many of their customers are hidden in third-party omnibus accounts," Sen. Peter Fitzgerald, R-Ill., said in a statement Wednesday. He said fund companies "must know their own customers to have any chance of enforcing their policies fairly and uniformly."

Daily Versus Weekly Disclosure

Fitzgerald and Rep. Paul Gillmor, R-Ohio, have introduced mutual fund reform bills that would require same-day disclosure of omnibus account information, an approach favored by the lobbying group. The SEC, in contrast, has proposed that intermediaries provide weekly information to mutual fund companies on omnibus account holders.

Besides giving fund companies more ammunition against market timers, the coalition said daily information on omnibus account holders would help fund companies check on the accuracy of sales charges, including any "breakpoint" discounts for larger investments, as well as other fees and dividend reinvestments.

Personal data on clients should be protected and mutual funds should use the information to boost enforcement and compliance, not marketing efforts, the group added.

The Investment Company Institute, the leading trade group for the $7.5 trillion mutual fund industry, declined to comment on the coalition's recommendations. It previously has endorsed the SEC's proposal on early redemption fees.

Securities Industry Association spokesman James Spellman said the brokerage industry trade group supports the SEC's proposed early-redemption fee, and favors other remedies, including having funds use fair value pricing, which would minimize the opportunities for market timers to profit on stale prices.

The SEC has proposed an early-redemption penalty, which it hopes will discourage market timers by cutting into their profits, and reimburse long-term fund shareholders for costs associated with timing trades.

The SEC's plan would require fund companies to impose a 2% fee on fund shares redeemed within five days. Yet the coalition found just two fund companies, MFS Investment Management and Putnam Investments, now apply a minimum five-day holding period. Nearly three-quarters have minimum holding periods of 30 to 90 days and some have a five-year minimum, the group found.

When calculating how to assess the penalty on early redemptions, the lobbying group favors the "last in, first out," approach. That is contrary to the current industry practice, in which 59% of the funds surveyed said they use "first in, first out" accounting on redemption fees. The lobbying group said the current approach gives market timers too much leeway and it recommended a stricter rule that would assume withdrawals are tapping the most recently deposited funds rather than earlier investments.

The study, which covers practices at fund giants such as Fidelity Investments and the Vanguard Group, is available online at www.investorscoalition.com.

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