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Omnibus Brokerage Accounts Decried

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8/10/2004 3:36 PM EDT

URL: <http://www.thestreet.com/markets/matthewgoldstein/10177529.html>

Omnibus trading accounts, the wholesale conduits through which Wall Street brokerages buy and sell mutual fund shares for their clients, provided crucial cover for the abusive strategy known as market-timing, critics contend. And these critics say the abuse won't completely end until brokerages are forced to provide more information about them.

The Coalition of Mutual Fund Investors says omnibus accounts, which are used on Wall Street to bundle customer trades, make it difficult for mutual fund companies to spot abusive trading patterns by specific investors. They provide a safe haven for rogue traders by cloaking their identities.

In an omnibus account, trades placed by thousands of different investors are submitted to a mutual fund company under a brokerage's name as one giant trade.

The coalition, a lobbying group formed last year by a Washington law firm in the wake of the mutual fund trading scandal, wants regulators to require brokerages to provide daily reports about all customer trades made through such an account. Without that information, the group contends, efforts by securities regulators to crack down on market-timing, or frequent trading, could prove fruitless.

"Omnibus accounts pose a huge impediment to mutual fund enforcement," says Niels Holch, the coalition's executive director and a partner in the Washington law firm **McGuinness & Holch**. "Omnibus accounts are places where market-timers hide."

Market-timing is one of the main trading abuses regulators have focused on in the nearly yearlong inquiry that has so far collected about \$2.4 billion in fines and restitution from a dozen major mutual fund companies. Regulators contend frequent trading in mutual fund shares hurts long-term investors because it drives up a fund's administrative costs and allows a handful of investors to skim profits.

A survey conducted by the coalition found that many of the biggest mutual fund families state in their prospectuses that they cannot adequately identify and monitor market-timers when trades are executed through omnibus accounts. The survey concluded that anonymous trading in omnibus accounts could undermine a **Securities and Exchange Commission** proposal to deter market-timing by requiring fund companies to impose a 2% redemption fee on all frequent trades.

"These shareholders are invisible to fund companies," says Holch, whose law firm also does lobbying for several Native American tribes, the Major League Baseball Players Association and a number of drug manufacturers. "I think this is a significant issue."

The SEC proposal on redemption fees does take steps toward addressing the anonymity that omnibus accounts provide to abusive trades. Besides the redemption fee, brokers would be required to give mutual funds a weekly accounting of all the customer trades made in an omnibus account.

But Holch says the SEC rule doesn't go far enough because that still allows an opportunity for fast-fingered market-timers to make frequent undercover trades from Monday through Friday. He suggests requiring brokerages to provide mutual funds with a daily update all of customer trades.

In response to the coalition's finding, Sen. Peter Fitzgerald (R-Ill.), who has introduced a bill to reform the mutual fund industry, issued a statement saying: "this study proves that greater transparency is not only helpful but absolutely essential in restoring the integrity of America's mutual fund industry."

The brokerage community, however, is likely to balk at providing a daily list of its customer's trades. Wall Street firms contend that omnibus accounts protect the privacy of all their customers, not just clients with nefarious motives.

Yet there's no doubt that omnibus accounts have allowed for a lot of mischief, and it's one area regulators have looked into during its investigation of **Bear Stearns** (BSC:NYSE) .

The mutual fund clearing operation at Bear Stearns, which handled trades for dozens of hedge funds and small brokerages implicated in the scandal, processed most of those trades through an omnibus account, say people familiar with Bear's operations. These people also say a group of Bear employees in the mutual fund clearing operation were known informally as the "timing desk," because they specialized in bundling market-timing trades.

In June, the SEC notified the big Wall Street firm that it will likely face civil charges for helping to facilitate the illicit strategies at the heart of the mutual fund trading scandal.