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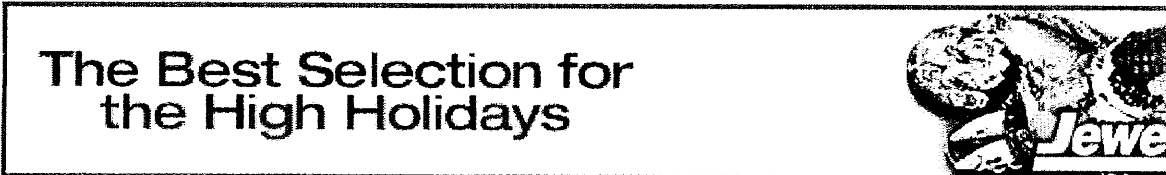

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YOUR MONEY: A WEEKLY GUIDE TO PERSONAL FINANCE: TAKING STOCK

What's right way to pay wronged investors?

Individuals' awards are often less than cost of sending check

By Laura Smitherman, a staff reporter for The Baltimore Sun, a Tribune Co. newspaper
Published September 17, 2006

State and federal regulators have won a string of settlements from Wall Street over trading scandals in the mutual fund industry, and more than $3 billion has been secured to be dolec wronged investors.

But determining who has a right to the money and who will actually get it is no easy task.

Should a mutual fund investor who lost pennies or dollars from trading improprieties see the if it costs more to process the claim and mail a check? How far should companies go to trac people who used to invest in a mutual fund if the cost to do so is subtracted from the settlen money?

A horde of consultants, financial firms and regulators are trying to sort out these issues. Anc handful of proposals for how to distribute the settlement money have been submitted to the Securities and Exchange Commission in recent months. But it could be many more months distributions are made to investors, and in the end, many of those who were victims might n included.

The numbers haven't been crunched, but one estimate floated by industry observers conter 90 percent of investors in the mutual funds that were harmed by improper market timing anc trading lost less than $10 each. Some plans generally would pay only those shareholders o' more than $10.

"There are just certain realities that dictate that some people who may be entitled to money get it because it's simply too expensive to get it to them," said Larry Goldbrum, general cour the Spark Institute, which represents retirement plan service providers.

The problems posed in the mutual fund cases are common to large-scale legal settlements, which justice often is measured in small dollar amounts and parties struggle to minimize exp and fees to maximize the amount left over for claimants.

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Those issues, though, are magnified by the complexities of the fund cases and the size of tl industry.

More than 90 million individuals own mutual funds, and about 8,000 mutual funds hold $9.4 in assets.

The SEC and New York Atty. Gen. Eliot Spitzer have negotiated many of the settlements, a several more cases could be brought. About a dozen companies have said they are still in negotiations with regulators.

Prudential Financial Inc.'s brokerage unit recently agreed to pay $600 million to settle charg former employees defrauded mutual fund investors by helping clients rapidly trade funds. U agreement $270 million will go to compensate the victims, with most of the rest going to the government.

The mutual fund scandals broke in 2003. The trading abuses enriched favored investment c and mutual fund companies, but cost ordinary fund investors because overall fund performa was hurt.

Late trading involves buying and selling mutual funds after trading is closed to other investo Market timing involves rapid trading that takes advantage of fund pricing changes.

The SEC is reviewing the plans that have been submitted thus far and is allowing the public submit comments before they are approved. Under the plans, independent consultants asce the damage done to each mutual fund, devised formulas to calculate shareholder losses, ar determined how--and whether--they should be paid.

"At the end of the day it has to be fair and reasonable; it doesn't have to be perfect," SEC spokesman John Nester said. "The administrators will do the best they can, and we oversee process to ensure they are, but tough calls have to be made."

A number of matters have to be resolved. A ruling from the Internal Revenue Service is pen over whether payouts would be taxable. And several groups, including the American Banke Association, have raised concerns about how the process would work.

Perhaps the most vexing obstacle is how to identify mutual fund holders who bought their sl through an intermediary such as a 401(k). Neat records are kept of people who buy and sel directly. But trades by those in a retirement plan, for instance, are typically consolidated in c order for thousands of participants.

Niels Holch of the Coalition of Mutual Fund Investors, an Internet-based advocacy group, sa some of the plans could unfairly penalize investors.

"We shouldn't spend $100 to give someone a dollar, I agree with that," he said, "but where t distribution plans draw the line may not be where the line should be drawn."

Sarah Miller, chief regulatory counsel for the bankers association, said more guidance is ne and called for a more standardized approach.

"We share the same goals in that we want to see the money paid to the rightful owners, but are so many of these settlement orders, and they all use different mechanisms," Miller said. think there is a real need for uniformity."

What's more important than the settlement money is that the legal cases have had a profou impact on the industry, said Don Phillips, a managing director at mutual-fund tracking firm Morningstar Inc.

"The fund industry is going to be a cleaner, better-lit playing field, and you are seeing a tren toward lower costs and fund boards that are more engaged," he said. "That's the real benef investors--not the $17.50 that's possibly going to be returned to you."

Laura Smitherman is a staff reporter for The Baltimore Sun, a Tribune Co. newspaper.

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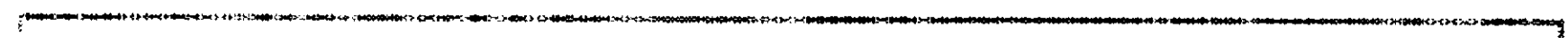

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