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SEC Urged to Centralize Fund Disbursements

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The SEC's failure to distribute most of the \$8.4 billion it has collected in regulatory settlement since 2002 has been roundly criticized by the Government Accountability Office. GAO says the SEC needs to centralize the administration of the fund.

More than \$2.6 billion of what is known as the Fair Fund has been distributed to date, according to Peter Bresnan, deputy director of the Division of Enforcement. Distributions have improved, he says, especially in the last year, when more than two thirds of the \$2.6 billion was returned to affected investors. However, the agency acknowledges it has a ways to go.

While the SEC and its critics agree that difficulty in finding investors, complexity of individual cases and tax issues have hampered disbursements, the GAO says a decentralized management style may be the culprit.

The SEC delegated responsibility for the management of the fund to its regional offices. These regional offices in turn were responsible for supervising independent consultants charged with creating distribution plans.

Fund shops involved in market-timing scandals contributed a substantial chunk, or about 38%, of the \$8.4 billion collected so far, according to Niels Holch, president of the **Coalition of Mutual Fund Investors**. The total also includes settlements from non-fund-related scandals, such as those involving Enron and WorldCom.

Some 27 mutual fund shops accounted for \$3.2 billion in collected funds related mainly to the market-timing scandals. Of that total, about \$2.7 billion has yet to be paid out, Holch says. "The decentralization of the Fair Fund program has made it difficult to have uniform policies and procedures in distributing the funds."

Bresnan says the SEC is in the process of creating a new central office and beefed-up staff to deal specifically with Fair Fund distribution. This represents a new administrative priority for the enforcement division.

The fund distribution "might not have been a [priority] in the past, but it needs to be today," Bresnan says. "Until the Fair Fund provision of Sarbanes-Oxley went into effect in 2002, we did not have funds of this magnitude that we needed to distribute, so we've had a steep learning curve."

Some industry attorneys say the SEC was not prepared to efficiently rectify an unprecedented event such as the mutual fund market-timing scandal.

"It is not reasonable to expect a government agency to handle one-time events with the level of efficiency that they do with their core responsibilities," says Gary Gardner, a lawyer in the Investment Management Division of **Pepper Hamilton**.

"The SEC is not in the business of recycling money," Gardner adds. "I think the GAO seems to be taking more of their fair share of potshots at the SEC."

The SEC may not have realized what it created in the wake of its aggressive campaign against mutual fund firms, says Todd Cipperman, an investment management lawyer at **Cipperman & Company**.

"It turned into much more of a management challenge than I think the [SEC] or anybody expected — an administrative Frankenstein monster they are having a hard time controlling" he says.

Larry Goldbrum, general counsel of **The Spark Institute**, says his organization has asked the SEC to require fund companies to accept financial responsibility for making retirement-plan-level allocations. Fund shops should also allow plan recordkeepers to allocate payments according to average share or dollar balances of the retirement plans that

are held in the fund, Goldbrum says.

The Spark Institute represents the recordkeepers and trustees who receive payments and then have to distribute the money to retirement plan participants.

While the SEC approved the organization's recommendation in some distribution plans, as subsequent distribution plans from different SEC regional offices were released, Spark still needed to remind the agency when it left out its recommendation, he says.

"The bottom line is for each distribution plan being developed, you have different people [SEC regional offices and consultants] developing them, and they are not necessarily coordinating with each other or following a consistent approach," Goldbrum says.

In March, SEC chairman Christopher Cox announced the agency's plan to centralize the Fair Fund program in a new office within the Division of Enforcement.

The office will be known as the Office of Distributions, Collections and Financial Information Management and will be composed of two separate groups: a Fair Fund distribution and collections unit and a financial information management unit. A new senior officer, two assistant directors and five additional staff will be part of the new office, to be based in Washington, D.C.

The new Washington office won't do all the distribution work, but will help with the different regional offices.

"In the past our distribution effort was more decentralized, and now with this new office and added resources, it is hoped we can speed up the process and make it more efficient," Bresnan says.

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