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SEC Considers Toughening Trading Rules for Managers

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The Securities and Exchange Commission is considering toughening its rules concerning personal trading by mutual-fund managers in the wake of the recent controversy surrounding the trading activities of **Dreyfus** fund manager Michael Schonberg.

The SEC's investment-management division is currently working out the final details of the proposed new rule and will soon present its complete proposal to the full commission for a vote. If the commission approves the proposal, it would broadly amend a rule under the Investment Company Act of 1940 by imposing new, stricter disclosure reporting requirements on mutual-fund managers' personal investment activities. The new rule would also force fund companies to disclose more information to individual investors about their policies on managers' trading.

Personal trading by fund managers isn't illegal. At issue here are potential conflicts between fund managers' own investment interests and those of their clients -- individual mutual fund investors. Many investors are unaware that fund managers also trade securities for themselves.

Fund companies are required to have their own codes of conduct relating to personal trading by their fund managers. The SEC proposal is designed to strengthen laws already on the books that prevent fund managers from misusing their jobs for personal gain.

"The rule is in final stages, and we expect to be recommending to the commission final action on the proposal in the near future," said Barry Barbash, director of the SEC's investment-management division. Mr. Barbash said the SEC has been toying with the idea of strengthening the rule since 1995, but he said the recent controversy involving the Dreyfus fund manager "has only convinced us that we are correct to finalize the rule as soon as we can."

When the SEC took up the issue about three years ago -- and charged several mutual-fund managers with civil fraud over their personal trading activities -- the proposal was never finalized amid pressure from the Investment Company Institute, the mutual-fund industry's main trade group. (Most of the fraud cases were resolved without the managers admitting or denying wrongdoing, although they resulted in civil fines.)

The ICI argued that forcing fund companies to disclose whether their fund managers may invest in the same securities that may also be held by the investment company "creates a pejorative implication" that the investment is suspect. Instead, the body made some nonbinding recommendations to the industry, including a ban on managers purchasing initial public offerings for their own account, and other reporting requirements.

The landscape shifted earlier this month, after well-known short-seller Manuel Asensio alleged that Mr. Schonberg personally benefited from some stock purchases he made for Dreyfus mutual funds he managed. Mr. Asensio was shorting the stock of **Chromatics Color Sciences International** and claimed that Mr. Schonberg invested heavily in the stock for the funds in order to manipulate the stock price "for his own personal gain." (Short sellers sell borrowed shares in the hope that the price will fall, allowing them to buy them back cheaply and pocket the difference.)

Mr. Schonberg, meanwhile, has been relieved of his duties as portfolio manager of **Dreyfus Agressive Growth Fund** and **Dreyfus Premier Aggressive Growth Fund** , but is still employed by the firm, which is owned by **Mellon Bank** . A Dreyfus spokeswoman said because of poor performance the firm began "diminishing" Mr. Schonberg's duties in April, and the company brought in another primary portfolio manager to take his place. She said Mr. Schonberg is now doing market analysis, and he is still part of the company's investment staff.

Mr. Schonberg didn't return telephone calls seeking comment. In a statement, the company said: "Dreyfus places the highest priority on its fiduciary responsibilities. Underlying this priority is our commitment that our strict policies and procedure that we have in place be followed in their entirety. Over the past few weeks, allegations have been made with respect to certain activities involving securities held in two different Dreyfus funds, and as a result, to ensure the integrity of Dreyfus, we have been conducting a thorough review of such activities. The review is not yet completed."

Meanwhile, the SEC has launched its own examination into whether or not Mr. Schonberg did anything wrong. If the agency determines that his personal-trading activities merit further review, the enforcement division could start a formal inquiry. "Under our policies, I can't comment on any particular matters," Mr. Barbash said. The Dreyfus spokeswoman said, "We do not respond to matters of that nature." The SEC has had a rule on its books for years governing fund-manager trading -- known as Rule 17j-1 -- which generally requires all investment companies to adopt codes of conduct governing personal trading. It also requires portfolio managers to file quarterly reports concerning their activities. The beefed-up rules under SEC consideration would make fund managers who move to a new firm disclose their investment portfolio to the new employer, and require fund companies to summarize their conduct policies in documents mailed to investors when they purchase a fund.

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Getting Personal

Fidelity Investments said that next month, 100,000 of its 401(k) account holders will begin receiving more personalized quarterly statements that, for the first time, will include personalized rates of return for the previous three months. By October, all 4.6 million of Fidelity's 401(k) plan participants will receive the new statements.

End of an Era

Sequoia Fund , the $4.4 billion, market-beating stock fund run by a passel of Warren Buffett disciples, finally made a stab at modern technology. It introduced a 24-hour touch-tone phone service, allowing customers to check fund prices and account balances around the clock.

The technology isn't new: Fidelity Investments introduced an early version of 24-hour telephone information in 1979. Only one of the 20 largest fund groups lacks 24-hour account information available by phone, according to Lipper Analytical Services -- and that group, Smith Barney, is sold by brokers. Investors in Sequoia don't generally have brokers to call about their account.

Sequoia says it introduced automated phone service to cut costs. The fund is closed indefinitely to new investors. But fielding queries about whether it was open was costing $2 a call to a live operator vs. 40 cents on the automated line. The line informs callers who aren't existing shareholders that the fund is closed.

In the 20 years through May 31, Sequoia gained 19.5% a year, beating the return of the S&P 500, with dividends, by about 2.5% a year.

Does the new service orientation at Sequoia mean the fund's devotion to stock picking is flagging? Richard Cunniff, the fund's vice chairman, responded to that question by laughing for a while.

Yields on Taxable Money Funds Mixed

Yields on taxable money-market funds were mixed, while those on tax-free money funds were slightly lower in the past week.

The average seven-day compound yield on taxable money funds eased to 5.12% from 5.14% in the week ended Tuesday, said IBC's Money Fund Report, an Ashland, Mass., newsletter. Compound yields assume reinvestment of dividends.

Assets of the 888 taxable funds rose $8.8 billion to a record $999.9 billion. Of that figure, institutional investors added about $9.6 billion.

The average seven-day simple yield on taxable funds slipped to 5.00% from 5.02%; the average 30-day simple yield inched up to 5.01% from 5.00%. The average 30-day compound yield held at 5.13%. Average maturity of taxable funds' investments, which include commercial paper (short-term corporate IOUs) and Treasury bills, stayed at 58 days.

The average seven-day compound yield on tax-free money funds dropped to 3.07% from 3.08% in the latest week. The latest yield is equivalent to a taxable 4.8% for an investor in the 36% tax bracket and to 5.08% for someone in the 39.6% bracket.

Assets of 442 tax-exempt funds fell $914.8 million to $171.9 billion. The average portfolio maturity rose to 39 days from 38 days.

IBC's Money Fund Report is published by IBC Financial Data Inc., a subsidiary of IBC USA (Publications) Inc.

--Pui-Wing Tam and Robert McGough