

Vanguard gives trend muscle

More firms likely to be adopting restrictions on frequent trading, but likely to be less restrictive

By Jenna Gottlieb
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The Vanguard Group Inc.'s new mutual fund trading restrictions will likely "open the floodgates" to other fund companies following in Vanguard's footsteps, Rick Meigs, founder of 401khelpcenter.com, predicts.

"Anytime you see Fidelity and Vanguard do something, others will jump on board," said Mr. Meigs, whose Portland, Ore., company provides information on defined contribution issues.

But he's not sure the other companies' policies will be as strict.

Beginning Sept. 30, Vanguard investors will not be allowed to buy shares of a Vanguard fund by phone or online within 60 days of selling shares in the same fund. Vanguard, in Malvern, Pa., currently allows investors to make unlimited roundtrips between funds, as long as it does not deem the trades large enough to have a negative impact on managing the funds.

Vanguard has one of the most restrictive policies of the fund companies that imposed restrictions following the mutual fund trading investigations by New York Attorney General Eliot Spitzer and the U.S. Securities and Exchange Commission.

Fidelity's guidelines

Fidelity Investments, Boston, set up guidelines effective last December that allow two roundtrip transactions for every fund within 90 days, and a total of four per year,

said spokesman John Brockelman. It had allowed four exchanges per year but did not include the 90-day cap, and exchange privileges could have been temporarily suspended or terminated if an investor exceeded that limit, he said. Dreyfus Corp., a subsidiary of Mellon Financial Corp., Pittsburgh, also allows four roundtrip trades per year, said Mike Dunn, spokesman.

OppenheimerFunds Inc., New York, adopted its new policy June 20 and allows shareholders to move between funds once in any 30-day period. A shareholder could transfer shares from a stock or bond fund into a money market fund at a time; however, all of the shares of the money market fund would then be blocked from further exchange for 30 days.

OppenheimerFunds executives instituted the policy because frequent purchases, redemptions and exchanges of fund shares can interfere with the fund manager's ability to manage investments efficiently and can increase the fund's transaction and administrative costs, said spokeswoman Jeaneen Pisarra.

In January, American Funds, owned by Capital Research and Management Co., Los Angeles, announced plans to limit shareholders to one fund exchange in an account in any 30-day period.

Mike Francis, president of Francis Investment Counsel LLC, Hartland, Wis., said the mutual fund industry is struggling with how to deal with sophisticated participants "gaming" the system. "While they may be in the minority, to buy and sell on a short-term basis, there's no better place to do it" than in a 401(k) plan, Mr. Francis said.

Because of the lack of government regulation, mutual fund companies are coming up with their own rules to discourage or outlaw short-term trading. “Whether it’s 90, 30 or 60 days, it’s a significant step for companies to make,” said Mr. Francis.

Who’s affected

Vanguard’s new policy will apply to participants in 401(k) plans, but will exclude investors in money market funds, short-term bond funds and exchange-traded funds. Also, the policy won’t apply to asset transfers and rollovers, check-writing redemptions, transactions by mail and certain automatic transactions. Vanguard first notified shareholders of the change June 30.

Fidelity’s policy excludes money market and exchange-traded funds.

It’s obvious that the industry needs to clamp down on frequent trading, said Mr. Francis, but “there’s been tension between wanting to set up rules to protect plan sponsors, and to not make rules so onerous that they don’t want to offer the plans anymore.”

Fund companies will try to formalize and institutionalize guidelines over time, he said, and will work closely with plan sponsors to review and monitor their plans for-frequent trading. “What you want to be clear on, market timing is not acceptable, and if participants are doing it, you as a fiduciary have a duty to stop it,” said Mr. Francis.

He doesn’t, however, expect the government to regulate mutual fund trading.