

MEMO# 7616

February 6, 1996

SEC STAFF GUIDANCE ON ""BUNCHING"" ORDERS AND ALLOCATION PROCEDURES

1 Pretzel & Stouffer (pub. avail. December 1, 1995). 2 See Memorandum to SEC Rules Members No. 63-95, Investment Adviser Members No. 42-95 and Investment Adviser Associate Members No. 37-95, dated September 15, 1995. February 6, 1996 TO: COMPLIANCE COMMITTEE No. 2-96 INVESTMENT ADVISER ASSOCIATE MEMBERS No. 4-96 INVESTMENT ADVISER MEMBERS No. 6-96 SEC RULES MEMBERS No. 8-96 RE: SEC STAFF GUIDANCE ON ""BUNCHING"" ORDERS AND ALLOCATION PROCEDURES

The staff of the Divisions of Investment Management and Market Regulation issued a letter providing general guidance on the rules and regulations governing an investment advisers ability to aggregate orders for the purchase and sale of securities on behalf of its clients, and the proper allocation of those trades among the clients.¹ The letter notes that the Division of Investment Management recently issued a no-action letter, SMC Capital, Inc. (pub. avail. September 5, 1995), in which the staff stated that the aggregation of orders among a registered investment company client and other clients that may be "affiliated persons" of the registered investment company (or affiliated persons of such persons) would not violate Section 17(d) of the Investment Company Act, provided that the investment company participates on terms no less advantageous than those of any other client.² In addition, consistent with an adviser's fiduciary duty under the Investment Advisers Act, an adviser that aggregates client orders must do so in a manner consistent with its duty to seek best execution of the orders, and must ensure that all clients are treated fairly in the aggregation and allocation. An adviser also must disclose to its clients its policies with respect to the aggregation of orders. The letter clarifies that an adviser does not violate its fiduciary duty to its clients merely by failing to aggregate orders for client accounts. In those instances, an adviser would have to disclose to its clients that it will not aggregate and the consequences of the failure to aggregate, such as potentially higher commissions. With respect to the allocation of aggregated trades, the letter notes that in the SMC Capital letter the allocation would be made and memorialized in writing prior to placing the order, although the allocation could be changed for good cause after the order had been placed. Any deviation from the original allocation would be explained in writing and approved by the adviser's compliance officer no later than one hour after the opening of the markets on the trading day following the day the order was executed. The letter indicates that there may be procedures other than those specified in the SMC Capital letter that advisers can use without violating Section 17(d) or Section 206. Amy B.R. Lancellotta Associate Counsel

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