

June 17, 1971

To Our Clients:

The Fidelity Fund brokerage recapture case, Moses v. Burgin, decided by the United States Circuit Court of Appeals for the First Circuit on June 4, 1971, is a landmark decision with respect to the fiduciary duties of mutual fund management companies and the directors of mutual funds. Specifically, the case holds that where recapture of brokerage is possible, it must be recaptured for the benefit of the fund and not used to reward brokers for the sale of fund shares. Broadly, the case can be interpreted as holding that the use of portfolio brokerage to reward brokers for the sale of fund shares for any purpose not of direct (and possibly exclusive) benefit of the fund is illegal. Negotiated rates and other changes in the NYSE commission structure and the final determinations as to institutional and non-member access and the separation of brokerage and investment management will be of overriding significance as to the necessity for mutual funds and other fiduciary institutions to recapture. Moses v. Burgin emphasizes the requirement that these

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matters be considered fully by the directors or trustees and that decisions be documented as having been reached on the basis of full information and the best interests of the shareholders or beneficiaries.

The decision in Moses v. Burgin, when coupled with the decision of the SEC hearing examiner in the Arthur Lipper -IOS over-the-counter brokerage rebate case reported in the Wall Street Journal and New York Times on June 16, 1971, indicates that the broker participants in reciprocity or rebate situations, that do not directly benefit the fund shareholders or beneficiaries, may be held liable for participation in breach of trust and accountable for damages and subject to disciplinary suspension or expulsion. Customer directed regional exchange reciprocal arrangements and all other arrangements for the "use" of "excess" brokerage by customers (other than for the direct benefit of fund shareholders or beneficiaries; these situations should be documented and reviewed by counsel) create the clear risk of civil liability and regulatory sanction.

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Investment advisors for private accounts and managers of private funds are again reminded of the desirability of making full disclosure of the use of brokerage to reward for research and other services, and to obtain specific authorization for such use.

M. Lipton

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