United States Securities and Exchange Commission

Public Comment on "Investment Company Governance"

17 CFR Part 270
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Comments Submitted:	VIA Electronic Mail
Comments Submitted to:	Nancy M. Morris Office of the Secretary Securities and Exchange Commission 100 F. Street, NE., Washington, DC 20549
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I. Introduction

I am commenting on the effects that the Securities and Exchange Commission's (the "Commission") proposed amendment, that requires investment companies ("funds") boards' to be comprised of at least 75 percent independent directors as well as requiring the boards to be chaired by an independent director, will have on the cost to funds and the protection of funds and fund shareholders. Furthermore, my comment discusses whether the proposed rule will promote efficiency, competition, and capital formation.

I thank the Commission for the opportunity to comment on the proposed rule and I respectfully submit the following thoughts. Generally, I am in strong support of the proposed regulation because it aims to protect the protection of funds and fund shareholders from conflict of interest issues that may arise otherwise.

I agree with the Commission that the implementation of the proposed regulation will protect the funds and fund shareholders while promoting efficiency, competition, and capital formation all at a miniscule cost burden on funds. My comment will illustrate this by providing a brief account of my background, summarize the events leading to the proposed regulation, make recommendations regarding the proposed regulation and then provide a brief conclusion.

II. Commentator's Background

I write as both a concerned citizen as well as a interested law student. I am currently a student at Villanova School of Law and next fall I will be advising clients on corporate issues relating to this proposed regulation. My past experience incorporates working at investment companies such as Vanguard and Prudential. Furthermore, I am a diligent and avid investor, who currently owns stock with Vanguard. I believe that my experience within these investment companies and my interests as a personal investor can provide a unique perspective of the implications that proposed rule 17 CFR Part 270 may have on both constituencies.

I have read the proposed rule in question and the related public comments. I thank the Commission in advance for reading and considering my thoughts. Further, I ask the Commission to please note that the comments and thoughts contained herein represent my views only and not necessarily the views or positions of the Villanova University School of Law or any other organization of which I am affiliated.

III. Background

On July 27, 2004, the Commission adopted amendments to the Exemptive Rules under the Investment Company Act to require funds that rely on one or more of those rules to adopt certain governance practices. Among other things, the amendments added two conditions for relying on the Exemptive Rules. The amendments require that, if a fund relies on at least one of the Exemptive Rules to engage in certain transactions otherwise prohibited by the Act, the fund must have a board of directors with (i) no less than 75 percent independent directors, and (ii) a chairperson who is an independent director. These amendments were adopted in the wake of a troubling series of enforcement actions involving late trading, inappropriate market timing activities, and misuse of nonpublic information about fund portfolios.

The two new conditions were challenged by the Chamber of Commerce, which submitted a petition for review to the United States Court of Appeals for the District of Columbia Circuit. The Court remanded to the Commission for its consideration two deficiencies that it identified in the rulemaking. First, the Court held that the Commission did not adequately consider whether the conditions would promote efficiency, competition and capital formation and the cost associated with the 75 percent independent board and the independent chairperson conditions. Second, the Court stated that Commission did not give the alternative of disclosing to the investors whether a board is independents or not adequate consideration.

IV. Analysis

I would like to reiterate that the troubling trading activities and other abuses perpetrated against mutual fund investors appear to have resulted from a systemic failure of internal controls and ultimately inadequate oversight by fund directors. I thus believe that the Commission's proposal to require that mutual fund chairpersons be independent from the fund's management is one of the most significant of the Commission's mutual fund related rulemaking activities. This section will focus on the effects this proposed regulation will have on the cost of individual funds, efficiency, competition, capital formation and the protection of funds and fund shareholders. Furthermore, it will analyze the alternative of simply advising potential investors of the composition of the board and will conclude that this alternative would not adequately accomplish the Commission's goal of protecting fund(s) shareholders.

A.) <u>The Cost Associated With the Fund Boards Being Comprised of at Least 75 Percent Independent Directors</u>

The amendments will impose additional costs on funds that rely on any of the Exemptive Rules by requiring that independent directors constitute at least 75 percent of the fund board or, if the fund board has only three directors, that all but one director be independent. As discussed in the Adopting Release, it is estimated that nearly 60 percent of all funds currently meet the 75 percent condition.[1] A fund that does not already meet this condition may come into compliance with the 75 percent condition by:

- decreasing the size of its board and allowing some interested directors to resign; or
- appointing/electing new independent directors either to replace interested directors (maintaining the current size of its board) or to increase the current size of its board.[2]

In the Adopting Release, the SEC stated that "our staff has no reliable basis for determining how funds would choose to satisfy this requirement and therefore it is difficult to determine the costs associated with electing independent directors."[3] The Court of Appeals noted, however, that "[t]hat particular difficulty may mean the Commission can determine only the range within which a fund's cost of compliance will fall,"[4] and directed that the Commission determine as best it can the economic implications of the rule. The following is a reliable basis upon which the SEC considered in formulating the range of costs associated with each of the two different ways, illustrated above, in which funds may choose to comply with the 75 percent condition.

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[1] Investment Company Governance, Investment Company Act Release No. 26520 (July 27, 2004) [69 FR 46378] (Aug. 2, 2004) ("Adopting Release")

[2] Under some circumstances a vacancy on the board may be filled by the board of directors. See section 16(a) of the Investment Company Act [15 U.S.C. 80a-16(a)] (board vacancy may be filled by any legal manner if immediately after filling the vacancy at least two-thirds of directors have been elected by fund shareholders).

[3] Investment Company Governance, Investment Company Act Release No. 26520 (July 27, 2004) [69 FR 46378] (Aug. 2, 2004) ("Adopting Release"). at 80.

[4] Chamber of Commerce of the United States of America v. SEC, No. 04-1300, slip op. (D.C. Cir. June 21, 2005) ("Slip Opinion"). at 15-16 ("That particular difficulty [of determining aggregate costs] may mean the Commission can determine only the range within which a fund's cost of compliance will fall, depending upon how it responds to the condition. . . .").

1.) Adding Independent Directors

Funds that elect to add independent directors in order to meet the 75 percent condition have two options. They may replace some interested directors with independent directors, or they may increase the size of the board. Funds that choose simply to replace interested directors with independent directors or that add additional independent directors may incur three kinds of costs. First, funds may incur initial and periodic costs of finding qualified candidates. Second, funds will incur annual compensation costs for the new independent directors. Third, funds could incur additional annual costs if new independent directors use additional services of independent legal counsel. Since smaller fund groups typically provide less compensation (for overseeing fewer funds) than larger fund groups (for overseeing more funds), compensation estimates are based on a range of potential costs.

It is understood that a majority of funds have eight or fewer directors.[5] Accordingly, the Commission concluded that most funds could appoint one or two independent directors in order to comply with the 75 percent condition.[6] For example, a board with eight directors could comply with the condition by replacing one interested director with an independent director.[7] However, acting conservatively to underestimate costs, this comment will assume that a fund would appoint three new independent directors.

Based on data from a 2004 survey of mutual fund directors' compensation,[8] the median annual salary for directors ranges from $111,500 (for boards that oversee a large number of funds) down to $12,500 (for boards that oversee from 1 to 6 funds). Consistent with the approach suggested by the Court the estimates are based upon the potential costs to an

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[5] See Management Practice Inc. Bulletin: Fund Directors' Pay Increases 17% in Smaller Complexes, 8% in Larger (June 2003) ("Boards are getting smaller with 60% having 8 directors or less.") (available at: http://www.mfgovern.com/); Management Practice Inc. Bulletin: More Meetings Means More Pay for Fund Directors (Apr. 2004) ("April 2004 MPI Bulletin") ("Boards are staying about the same overall size, with a slight decrease in the number of interested directors, which facilitates a new 75% independent requirement.").

[6] A fund that currently relies on any of the Exemptive Rules would already have a majority of independent directors on the board. See Role of Independent Directors of Investment Companies, Investment Company Act Release No. 24816 (Jan. 2, 2001) [66 FR 3734 (Jan. 16, 2001)].

[7] An 8 member board of a fund that relies on at least one Exemptive Rule currently must have at least 5 independent directors. By replacing an interested director with an independent director, 6 out of 8 (75%) would be independent. By replacing two interested directors with two independent directors on a 7 member board (which must have at least 4 independent directors), 6 out of 7 (86%) would be independent.

[8] See Management Practice Inc. Bulletin: Fund Directors' Pay Increases 17% in Smaller Complexes, 8% in Larger (June 2003). The information provided in the Bulletin "summarizes 2003/4 findings of the Mutual Fund Directors' Compensation and Governance Practices survey with data drawn from public documents of 290 complexes, representing 1,620 directors/trustees and the confidential responses of participating complexes." Thus, the survey may include compensation information concerning both independent and interested directors.

individual fund. Thus, the annual compensation cost per fund for appointing one independent director could range from $1,593 (for boards that oversee a large number of funds) to $12,500 (for boards that oversee only one fund).[9] Accordingly, if a fund were to appoint three independent directors, the Commission estimates that these annual compensation costs could range, on a per fund basis, from $4779 (for boards that oversee a large number of funds) to $37,500 (for boards that oversee one fund).[10]

Furthermore, the costs to recruit an independent director may equal the independent director's first year salary.[11] This cost may be incurred initially when the independent directors are first appointed, and periodically thereafter when, from time to time, an independent director is replaced. The need to replace a director will on average occur no more often than once every five years.[12] Thus, the initial per fund cost for recruiting services for three independent directors could range from $4,779 (for boards that oversee a large number of funds) to $37,500 (for boards that oversee one fund). Based on turnover every five years, the annual cost per fund thereafter to replace independent directors could range from $956 to $7500 respectively.[13]

However, funds will incur additional costs because of increased reliance by new independent directors on the services of independent legal counsel. On average, according to the Commission the new independent directors will use an additional 30 hours annually of independent legal counsel services. The average hourly rate for an independent counsel is $300, which yields a total cost of $9000 annually, per board.[14] Thus, the range of costs for additional independent counsel services could range from $9000 per fund (for a board that oversees one fund) to $129 per fund (for a board that oversees a large number of funds).[15] Based on this data, the total costs in the first year, for funds that appoint three new independent directors, could range from $9687 per fund

[9] These annual estimates of the cost of one independent director are based on the following calculations: ($111,500 / 70 funds = $1593); ($12,500 / 1 fund = $12,500). In considering the range of costs per fund, we divided the median salary for a director overseeing a large number of funds (70 or more) by 70 funds, and the median salary for a director overseeing a small number of funds (1 to 6) by 1 fund. The range of funds was based on data provided in the April 2004 MPI Bulletin, supra note 19.

[10] These annual estimates of the cost per fund are based on the following calculations: ($1593 x 3 directors = $4779); ($12,500 x 3 directors = $37,500).

[11] See, e.g., Andrea Felsted, Headhunters Feel the Heat in Quality Quest: Shareholder Reaction to Sainsbury's Choice of a Chairperson-Designate has Shed a Harsh Light on a Secretive World, FINANCIAL TIMES, Feb. 21, 2004, at 5. This one-time cost would be shared among the funds that the director oversees.

[12] See, e.g., supra note 19. (noting that, based on a 2000 survey, "[s]erving trustees have a median age of 62 with a median of 10 years of service.").

[13] These estimates are based on the following calculations: ($4779 / 5 = $956); ($37,500 / 5 = $7500).

[14] The $300 per hour estimated billing rate is one we have used in recent rulemakings. See, e.g., Disclosure Regarding Nominating Committee Functions and Communications Between Security Holders and Boards of Directors, Securities Act Release No. 8340 (Nov. 24, 2003) [68 FR 69204 (Dec. 11, 2003)] at n.149.

[15] These estimates are based on the following calculations: ($9000 / 1 = $9000); ($9000 / 70 = $129).

(for boards that oversee a large number of funds) to $84,000 per fund (for boards that oversee one fund).[16] Annual costs in subsequent years would decrease to a range of $5864 per fund (for boards that oversee a large number of funds) to $54,000 per fund (for boards that oversee only one fund).[17]

Funds that must obtain shareholder approval for new independent directors (whether to replace interested directors or to increase the size of the board) will incur additional costs of soliciting proxies from shareholders. The Commission estimates the average costs of soliciting proxies as $75,000 per fund. If a fund must obtain shareholder approval for three new independent directors, the initial costs to add the directors could range from $84,687 per fund (for boards that oversee a large number of funds) to $159,000 per fund (for boards that oversee one fund). And as discussed above, costs would decrease in subsequent years to a range of $5,864 per fund (for boards that oversee a large number of funds) to $54,000 per fund (for boards that oversee only one fund).

Accordingly, the Commission has estimated current first year costs of the condition for funds in which the board appoints three new independent directors. These costs could range from $11,624 per fund (for boards that oversee a large number of funds) to $100,800 per fund (for boards that oversee one fund). The Commission has further estimated that the current first year cost for funds that elect three new independent directors could range from $101,624 per fund (for boards that oversee a large number of funds) to $190,800 per fund (for boards that oversee one fund). Whether the new independent directors are appointed or elected, ongoing costs could range from $7,037 per fund (for boards that oversee a large number of funds) to $64,800 per fund (for boards that oversee one fund).

2.) Decreasing Interested Directors

The second option funds can take is to decrease the size of their boards and allow some interested directors to resign. Funds that follow this option are likely to incur, at most, only minimal direct costs. The decision to reduce the size of the board and eliminate one or more interested directors from the board would likely be made at a previously scheduled board meeting. Because this option is the simplest of the two options and imposes the lowest direct costs, it is likely that many, if not most, funds will choose to comply with the 75 percent condition by using this option. There is the possible non-monetary cost of the loss of experience on the board. In other words, having fewer interested directors on the board might decrease the expertise of the board. However, I agree with the Commission as it discussed in the Adopting Release, that nothing in the Exemptive Rule amendments would prohibit interested persons from participating in

[16] These estimates are based on the following calculations: ($4779 (first year compensation) + $4779 (recruiting costs) + $129 (independent counsel costs) = $9687); ($37,500 (first year compensation) + $37,500 (recruiting costs) + $9000 (independent counsel costs) = $84,000).

[17] These estimates are based on the following calculations: ($4779 (annual compensation) + $956 (recruiting costs) + $129 (independent counsel costs) = $5864); ($37,500 (annual compensation) + $7500 (recruiting costs) + $9000 (independent counsel costs) = $54,000).

board meetings, if the directors decide to include them in those meetings. Thus I believe that the reduction in the number of interested directors will likely result, at most, in only minimal direct costs.

B.) <u>The Cost Associated with Fund Boards Being Chaired by an Independent Director</u>

Simply increasing the number of independent directors is not enough. It is essential that fund boards also have an independent chairperson. With the chairpersonship comes the power to set the agenda, primary responsibility for determining what information is provided to the board by the fund advisor and other service providers, and the ability to guide board discussion of key issues. By allowing an interested person to be chair would in turn serve to undermine the 75 percent independence requirement. Therefore it is quintessential for the chairperson to be independent.

Nonetheless, with the independent chairpersons come the additional costs of hiring them as well as adding staff in order to support them. In addition to the monetary costs, some have raised, as a possible non-monetary cost, the loss of experience on the board if the interested chairperson were to resign from the board. These different issues are contemplated below.

1.) Cost of Additional Staff

Several commenters suggested that an independent chairperson might decide to hire staff to help fulfill his or her responsibilities. Although it cannot determine how many independent chairpersons would require the hiring of additional staff to support them, I agree with the Commission's estimates of the costs that fund boards may incur as a result of hiring additional staff in the following.

I agree with Commission that independent chairpersons will be expected to hire no more than two staff employees, consisting of one full-time senior business analyst and one full-time executive assistant. Nonetheless, these costs will be borne primarily by larger fund complexes, and independent chairpersons at smaller complexes will rarely choose to hire additional staff. The Commission has estimated the costs of retaining these personnel based on salary surveys conducted by the Securities Industry Association ("SIA"), a source on which the Commission commonly relies upon in its rulemakings. The SIA found the average salary (including bonus) of a senior business analyst to be $136,671. The SIA found the average salary of an executive assistant (including bonus) to be $73,088. However, these salaries need to be adjusted upwards by 50 percent to reflect possible overhead costs and employee benefits. With this the salary amounts to $205,007 (for the senior business analyst) and $109,632 (executive assistant) respectively. Thus, the hiring of both a full-time senior business analyst and a full-time executive assistant for an independent chairperson would total approximately $314,639 for each board. This cost can be expressed on a per fund basis, which is calculated to be $42,519.

Some commenters suggested that another cost of the amendments could result from increased reliance by the independent chairperson on the services of independent legal counsel. On average, the independent chairperson will use independent legal counsel a total of 50 hours a year more under the proposed rule. The Commission has estimated that the average hourly rate for an independent counsel is $300, which yields a total cost of $15,000 annually, per board. This amounts to $2,027 per fund. Therefore, according to the Commission the overall cost of additional staff is estimated to be around $44,546. This is a small price to pay to have a chairperson who is acting in the best interest of the shareholders.

2.) Increased Compensation for an Independent Chairperson

The estimated cost associated with the compensation an independent chairperson is diminutive compared to the benefits (previously stipulated) added to the funds. The Commission calculated that the compensation for an independent chairperson may be from 25 to 50 percent higher than the compensation of other directors. In order to calculate maximum likely costs and avoid understating those costs, the Commission uses the assumption of the higher end of the range, i.e., a 50 percent premium, and takes into account the 20 percent increase reflecting possible increased compensation costs. Therefore, based on the estimates discussed above regarding compensation for fund independent directors, the Commission estimated that the additional ongoing compensation cost, and other cost increases, of appointing an independent director as chairperson could range from $1,147 to $9,000 each year, per fund. This again proves to be a small sum relative to the benefits.

3.) Lack of Experience

In addition to the monetary costs, critics have also commented on the loss of experience on the board if the interested chairperson were to resign from the board. This concern however can be mitigated by the fact that there will be additional staff supporting the independent directors as well as the notion that the interested chairperson typically is one of the most senior officers of the fund's investment adviser, which has a direct interest in the operations of the fund. Therefore, I agree with the Commission in anticipating that the interested chairperson is unlikely to resign from the fund's board, and will likely continue to participate actively in board meetings even though he no longer functions as the chairperson.

C.) <u>Promotion of Efficiency, Competition and Capital Formation</u>

As noted by the Court, the Commission must consider the impact of the costs of compliance with the two conditions on funds' efficiency, competition and capital formation. I agree with the Commission (for the previous mentioned reasons) in concluding that the costs of the 75 percent condition and of the independent chairperson condition are extremely small relative to the fund assets for which fund boards are responsible, and are also small relative to the expected benefits of the two conditions. The minimal added expense of compliance with these conditions will have little, if any, adverse effect on efficiency, competition and capital formation. Indeed, complying with the two conditions by funds that rely upon the Exemptive Rules will help increase investor confidence, which may lead to increased efficiency and competitiveness of the U.S. capital markets. Furthermore, this increased market efficiency and investor confidence may encourage more efficient capital formation.

With respect to the 75 percent condition, even for funds that elect to add independent directors and are required to solicit proxies, the costs are minor compared to the amount of assets under management. For funds that choose to comply with the 75 percent condition simply by decreasing the size of the board, the costs are insignificant. For funds that appoint three new independent directors, using the data from the 2004 survey and adding a 20 percent cushion as discussed above, the ongoing annual costs range from $64,800 per fund, for boards that oversee only one fund, down to $7,037 per fund, for boards that oversee a large number of funds. Start-up costs in the first year are somewhat more per fund: from $100,800 per fund for boards that oversee only one fund, to $11,624 per fund for boards that oversee a large number of funds. For funds that cannot appoint the new directors and must solicit proxies, the first year costs per fund increase to $190,800 for boards that oversee only one fund, and to $101,624 for boards that oversee a large number of funds. Using any of the options, the costs per fund will be no more than a very small fraction of the fund assets for which the fund boards are responsible.

The costs of the independent chairperson condition are likewise small. Even if the independent chairperson hires two full-time staff (at New York salaries), and uses 50 hours of additional independent legal counsel, the total is only $329,639, which would be divided among the number of funds overseen by the independent chairperson. And the additional per fund compensation received by the independent chairperson could range from $9,000 for an independent chairperson who oversees a single fund, down to $1,147 for an independent chairperson who oversees a large number of funds. Even using the highest additional compensation figure, the average fund will incur a total cost for staff, legal counsel and additional compensation of only $47,220.

Whether the two conditions are viewed separately or together, even at the high end of the ranges, the costs of compliance are minimal. The Commission also noted that the ranges of costs considered above represent the high range of potential cost of compliance for any individual fund. The average cost per fund to the industry as a whole will likely be much lower. At the time the Commission adopted the rule amendments, 60 percent of funds already complied with the 75 percent condition and will incur no additional cost as a result of the implementation of that condition. Moreover, few boards are likely to appoint or elect as many as three new independent directors. Most are likely to decrease the size of their board or add one or two new directors. The Commission’s highest cost estimates are for boards that oversee only a single fund, which is an atypical situation. It would be unlikely that such a board would choose the more costly options of adding as many as three new directors and hiring two full-time staff to assist the independent chairperson.

Moreover, these costs are slight in relation to the very important benefits of the two conditions, as more fully discussed in the Adopting Release. The 75 percent condition is intended to promote strong fund boards that effectively perform their oversight role.

Enhanced oversight by a strong, effective and independent fund board will serve to protect funds and their shareholders from abuses that can occur when funds engage in the conflict-of-interest transactions permitted under the Exemptive Rules. This will increase investor confidence in fund management and promote investment in funds. While these benefits are not easily quantifiable in terms of dollars, I agree with the Commission that they are substantial, particularly in comparison to the estimated cost of compliance. The independent chairperson condition will provide similar benefits. The chairperson of a fund board can have a substantial influence on the fund board agenda and on the fund boardroom's culture. An independent chairperson will advance meaningful dialogue between the fund adviser and independent directors and will support the role of the independent directors in overseeing the fund adviser. Moreover, an independent board led by an independent chairperson is more likely to vigorously represent investor interests when negotiating with the fund adviser on matters such as fees and expenses. These cumulative benefits fully justify the costs associated with the rule amendments.

Furthermore, the proposed rules amendments to the Exemptive Rules will not have a significant adverse effect on efficiency, competition or capital formation because the costs associated with the amendments are minimal and many funds have already adopted the required practices. By promoting investor confidence in the fairness and integrity of the individuals that monitor investment companies, the proposed regulation helps promote investor confidence in our markets at a minimal cost. Investors will likely be more willing to effect transactions in those markets, which in turn will help to increase liquidity and to foster the capital formation process. Increased investor confidence in the integrity of mutual funds also will lead to increased efficiency and competitiveness of the U.S. capital markets.

D.) <u>The Alternative?</u>

The Court of Appeals also stated that the Commission did not give adequate consideration to an alternative to the independent chairperson condition, discussed by the two dissenting Commissioners, that "each fund be required prominently to disclose whether it has an inside or an independent chairperson and thereby allow investors to make an informed choice." As discussed below, I agree with the Commission that providing information to enable an informed investment decision -- would not adequately protect fund investors from the potential abuses inherent in the conflict-of-interest transactions. This conclusion is reached in light of the nature of investment companies and the purposes of the statutory prohibitions to which they apply.

As the Commission explained in the release proposing the 2001 amendments to the Exemptive Rules, funds are unique in that they are organized and operated by people whose primary loyalty and pecuniary interest lie outside the enterprise. This "external management" structure presents inherent conflicts of interest and potential for abuses. The investment adviser firms that manage the funds have interests in their own profits that may conflict with the interests of the funds they manage. In many cases, as the Commission has noted, fund boards continue to be dominated by their management companies.

Even with respect to conflicts of interest on the part of managers of investment companies, disclosure in some cases can provide important protections. In the context of the subject of this rulemaking, for example, disclosure may enable fund investors to decide whether to invest in a fund that does not have an independent chair. But the utility of such disclosure is limited. Disclosure concerning conflicts of interest on the part of fund managers and the potential for self-dealing by them does not prevent the managers from putting their interests ahead of investors' interests. Disclosure does not prevent them from engaging in self-dealing.

The objective of limiting these conflict-of-interest prohibitions will best be served by strengthening -- through enhanced independent oversight -- investor confidence that those charged with managing their fund will act in the investors' interests. Under these circumstances, I agree with the Commission that disclosure alone is not sufficient to adequately protect a fund investor against the serious risk that the managers of his or her investment will engage in self-dealing.

Moreover, even assuming that meaningful disclosure would be an adequate alternative to a requirement of an independent chair, there are obstacles to making disclosure that would be meaningful. I doubt the sufficiency of merely disclosing that a fund does not have such a chair. For prospectus disclosure to be meaningful, investors considering a fund would have to be informed of the conflicts of interest faced by fund advisers, the complex role of the fund board in managing those conflicts, and the potential consequences to investors of the failure of fund boards to protect against conflicts. It would be difficult to provide meaningful disclosure of these matters.

I also agree with the Commission that the chairperson can play an important role "in establishing a boardroom culture that can foster the type of meaningful dialogue between fund management and independent directors that is critical for healthy fund governance." A board can most effectively manage the conflicts of interest inherent in these transactions where the board culture encourages rather than stifles open and frank discussion of what is in the best interest of the fund. This is especially true in connection with the conflicts of interest presented by these transactions because the best interest of the fund frequently is different from the best interest of the fund's management company. Similarly, as the Commission stipulated, the chairperson of a fund board "is in a unique position to set the tone of meetings and to encourage open dialogue and healthy skepticism." An independent chairperson is better equipped to serve in this role. An independent chairperson also can play an important role in serving as a counterbalance to the fund's management company by providing board leadership that focuses on the long-term interests of investors.

None of these benefits can be achieved merely by disclosure. I agree with the Commission that it is necessary and appropriate in the public interest and consistent with the protection of investors in having a 75 percent independent board as well as an independent chairperson.

V. Conclusion

I would like to reiterate that the troubling trading activities and other abuses perpetrated against mutual fund investors appear to have resulted from a systemic failure of internal controls and ultimately inadequate oversight by fund directors. I thus believe that the Commission's proposal to require that mutual fund chairpersons be independent from the fund's management is one of the most significant of the Commission's mutual fund related rulemaking activities.

As the Commission explained in its release proposing the rule, "A boardroom culture conducive to decisions favoring the long-term interest of fund shareholders may be more likely to prevail when the board chairperson dos not have the conflict of interest inherent in his role as executive of the fund adviser." As Mr. John C. Bogle has observed, mutual fund investors are simply not best served when "de facto control of a fund's board is held by the firm that earns its profits from being the principle provider of the services required for the funds existence."

Furthermore, an independent chairperson would set the proper "tone at the top" among those in charge with overseeing the fund's internal controls and compliance by making it clear that the interests of fund shareholders, rather than that of management, are paramount. An independent chairperson can foster the type of meaningful dialogue between fund management and independent directors that is critical for healthy fund governance.

Also, mutual fund investors stand to benefit from a stronger negotiator on their behalf when it comes to keeping fees that come out of their pockets low. Stronger negotiators by the representatives of fund shareholder, that is, independent directors of the fund, should reduce the fees that investors pay. In this regard, I again agree with the Commission's statement in the proposing release that "a fund board may be more effective when negotiating with the fund adviser over matters such as the advisory fee if it were not at the same time led by an executive of the adviser with whom it is negotiating." Warren Buffett said it well – "Negotiating with oneself seldom produces a barroom brawl."

To conclude, I agree with the Commission proposed regulation. The proposed regulation promotes investor confidence in the individuals that monitor investment companies. This in turn helps promote investor confidence in our markets. Investors will likely be more willing to effect transactions in those markets, which in turn will help to increase liquidity and to foster the capital formation process, all at a miniscule cost to the fund. This increase in investor confidence in the mutual funds will also lead to increased efficiency and competitiveness of the U.S. capital markets. For the aforementioned reasons the implementation of the proposed regulation will protect the funds and fund shareholders while promoting efficiency, competition, and capital formation all at a miniscule cost burden on funds

I urge the Commission to adopt the proposed rule, without amendment. It is vitally important for the Commission to help restore the confidence of mutual fund investors. Nothing sends a stronger message to the investing public than corporate governance reform that places the interests of mutual fund investors first.

Again, thank you for taking the time to read this comment. While I realize the deadline for submission of public comments has passed, I ask the Commission to nevertheless please consider the recommendations contained herein in hopes that they will aid the Commission's formation of the final rule. I would be happy to address any questions raised by my comment.