Fidelity Investments

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Mr. Paul F. Roye
Director, Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Dear Paul:

Following up our recent conversation, I am writing on behalf of Fidelity Investments to convey our deep concern over the Commission's intention to consider proposing a rule that would, in effect, prohibit fund directors, including disinterested directors, from exercising their informed business judgment to appoint any individual of their choosing to serve as board chairman, whether the director selected happens to be interested or disinterested It is our strongly held view that so limiting the discretion of board directors simply is not good public policy. Rather than strengthening the hand of disinterested directors, it would undermine the stature and effectiveness of all fund directors, including disinterested directors, by depriving them of the ability to reach informed business judgments after taking into account the unique facts and circumstances that apply to different boards and different fund complexes.

We are taking this opportunity to urge that the Commission consider alternatives to a government-imposed limit on the choices available to fund directors when selecting a board chairman. We ask that the Commission, if it proposes a rule requiring a disinterested board chairman for mutual funds, at the same time seek public comment on alternatives to such a requirement, and in this letter we offer some suggestions.

ACTS to DTSW

Alternatives to a Disinterested Chairman Requirement

To enhance the ability of a fund's disinterested directors to perform their responsibilities under the federal regulatory scheme on behalf of fund shareholders, we suggest that the Commission consider, and seek comment on, whether one or more of the following measures are appropriate, even preferable, alternatives to a rule that would deprive directors of the discretion to select any individual of their choosing to serve as board chairman:

(1) Disinterested directors should constitute no less than 2/3 of a fund's board;

(2) Disinterested directors should have sole authority to set their own compensation. This authority, coupled with their existing authority to select and

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nominate those who will serve as disinterested directors, will reinforce the ability of disinterested directors to carry out their responsibilities in an independent manner;

(3) A fund's board should annually elect the board chairman, with separate votes by the board as a whole and by the disinterested directors. This is consistent with the approach mandated by the Investment Company Act for the approval and annual renewal of a fund adviser's management contract;

(4) The election of board chairman should be submitted to fund shareholders for ratification at any meeting of shareholders called for the election of fund directors;

(5) The agenda for every regularly scheduled board meeting should be approved separately by the disinterested directors; and

(6) The disinterested directors should separately approve the formation and charter of each board committee, as well as the appointments of members to each committee.

The foregoing measures, in our view, would ensure that disinterested directors, forming a supermajority of a fund's board, would exercise separate authority over those aspects of board governance – the setting of agendas, the creation of board committees, and assignment to board committees – that bear directly upon the effective functioning of fund boards. With these measures in place, we submit that no additional public policy would be served by prohibiting disinterested directors from selecting an interested director as board chairman. Indeed, such a selection in many instances is likely to be in the best interests of fund shareholders by promoting administrative efficiencies and drawing upon the experience and expertise of an individual within the fund industry.

Preserving Flexibility and Choice for Fund Boards

It is noteworthy that the Directors Committee of the ICI has endorsed an approach very similar to ours, and by its letter of December 31, 2003, has urged the Commission to preserve the ability of fund boards to exercise the full range of their business judgment in choosing a board chairman. Members of the Directors Committee who are disinterested directors far outnumber those who are interested directors.

Our views, in fact, are fully consistent with the Commission's own position, set forth in your testimony before the House Financial Services Subcommittee on Capital Markets on June 18, 2003. Speaking for the Commission, you pointedly did *not* endorse the provision of H.R. 2420 which would have deprived fund boards of authority to select an interested director to serve as chairman. In light of the bill's requirement that at least two-thirds of a board consist of disinterested directors, you noted that this would

empower disinterested directors to select one of their own as board chairman if they so desire.[1] We also believe the Commission was correct when you noted that a supermajority requirement for disinterested directors would ensure that those directors would be free to exercise their business judgment regarding the selection of any director to serve as board chairman. We submit that none of the well-publicized problems in the mutual fund industry that have been brought to light in the last six months negates the correctness of the Commission's position expressed last June.

We also urge the Commission to consider the implications for the rest of Corporate America that would flow from a governmental fiat that mutual fund boards, without exception, be chaired by a disinterested director -- regardless of whether a fund's directors, left to their own business judgment, might conclude that the interests of shareholders would be best served by an interested director serving as chairman. Corporate governance experts express widely differing views on the merits (and demerits) of an independent director chairing corporate boards.

Professor Charles Elson, Director of the Center for Corporate Governance at the University of Delaware, College of Business and Economics, has expressed serious reservations over the "non-executive" chairman (even in the absence of a governmental rule that would require this result):

> "[T]he problem with a non-executive chairman is that you create two leadership points. You effectively create two power centers. I think it becomes very confusing within the organization as to who reports to whom, and I think it creates, effectively, two chiefs.... I don't think it works particularly well in the UK. They have had that system for years, and I don't see UK companies being held up as paragons of corporate governance or performance owing to that structure."[2]

We are aware that mutual funds are unique in that their operations are externally managed by investment advisers and other service providers, and that this structure gives rise to potential and actual conflicts of interest. Mutual fund boards, and the disinterested directors of those boards, have singular responsibilities under the Investment Company Act to act for the benefit of fund shareholders in resolving these conflicts of interest.

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[1] Testimony of Paul F. Roye, Director, Division of Investment Management, U.S. Securities and Exchange Commission, Concerning The Mutual Funds Integrity and Fee Transparency Act of 2003, H.R. 2420, Before the House Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, Committee on Financial Services (June 18, 2003) at 18:

> "We agree that there may be benefits to having an independent director serve as the board chairman, such as the ability to control boardroom agendas and manage the flow of information to members of the board. We would note, however, that by increasing the representation of independent directors on fund boards, the Bill clearly would empower independent directors to select one of their own as chairman **and to use their judgment as to who should serve as chairman**." (emphasis added)

[2] Directorship. "A Director-Professor Speaks Out," (Nov. 1998 – January 1999) at 1-2.

To assume, however, that conflicts of interest arising within operating companies somehow pose lesser risks to shareholders or are less acute than those faced in the fund industry, simply because operating companies have "internal" management is to ignore the history of corporate governance in this country -- a history punctuated by the debacles of recent years, such as Enron, WorldCom and Tyco, that have imposed heavy losses on mutual funds and other investors.

We submit that there is no principled distinction between mutual funds and other companies on the question of whether board directors should be free to exercise their informed business judgment to select any member of the board to serve as its chairman. It is unwise public policy for the mutual fund industry and unwise for every other U.S. industry as well to impose a "one size fits all" independent chairman requirement. The Commission's unilateral action to deprive fund boards of the discretion to choose their chairmen will have unmistakable implications for the corporate boards of all other American companies.

We hasten to acknowledge that fund directors might well decide upon a disinterested director to serve as board chairman in particular cases, as they have already done in a number of fund complexes. We also acknowledge the possibility that the selection of disinterested directors to serve as board chairmen may emerge over time as the norm in the fund industry. If this reflects the informed business judgment of fund boards, and their disinterested directors, this is as it should be. Fund boards, not the government, should make these decisions.

On the other hand, for over half a century, the Fidelity Funds Board has reached the informed judgment that the Funds' shareholders have been well-served -- indeed, extraordinarily well-served – through the strong leadership and vision of the Johnson family, the founders of the Fidelity Funds. In recognition of this, the Board chose as its chairman, Edward C. Johnson 2nd and has chosen to be led by its current chairman, Edward C. Johnson 3rd. It is open to question whether all of the innovations that have advanced the interests of Fidelity Funds' shareholders over so many years, including the enormous commitment to the use of technology, could have been achieved if the Trustees of the Fidelity Funds had been prohibited from exercising their judgment in choosing the Board's chairman. We respectfully suggest to the Commission that it not deprive the Fidelity Funds Board – or the board of any other fund complex – of the authority, and responsibility, of choosing its chair.

Very truly yours,

Eric Roiter

cc: Hon. William H. Donaldson
Chairman of the Securities
and Exchange Commission

Hon. Paul Atkins
Commissioner

Hon. Roel Campos
Commissioner

Hon. Cynthia A. Glassman
Commissioner

Hon. Harvey Goldschmid
Commissioner

Robert Plaze
Associate Director

Douglas Scheidt
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