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TO: Public Comment File No. S7-03-04

FROM: Jennifer B. McHugh JBM
Senior Advisor to the Director
Division of Investment Management ("IM")

DATE: June 7, 2004

On June 3, 2004, Mark S. Howard, Senior Vice President and Life/IMCO/FPS General Counsel of USAA, and Dick Zucker, an independent director of the USAA mutual funds, met with staff members of the U.S. Securities and Exchange Commission to discuss issues relating to the Commission's outstanding fund governance proposals. The following Commission staff members attended the meeting: Paul Roye, Director, IM; Robert Plaze, Associate Director, IM; Jennifer McHugh, Senior Advisor to the Director, IM; and Martha B. Peterson, Counsel to the Chairman.

During the meeting, Messrs. Howard and Zucker discussed in greater detail the viewpoints contained in USAA's comment letter on the fund governance proposal (see File No. S7-03-04), including their opposition to the proposed independent fund chairman requirement. Messrs. Howard and Zucker's talking points from the meeting are attached.

USAA®

USAA POSITIONS ON SEC
INVESTMENT COMPANY GOVERNANCE PROPOSALS

USAA expresses the following key points on the SEC's investment company governance proposals:

- **Support strong enforcement of existing laws and regulations as primary remedy for industry wrongdoings.** Costs of additional regulations will ultimately result in higher costs to fund shareholders or job reductions in fund industry.

- **Continued increase of independent director duties will cause status over time to drift from its appropriate role of oversight to management.** Such duties as determining Compliance Officer compensation could place directors in status as employers with corresponding responsibilities and potential liabilities.

- **Opposes mandatory independent chair requirement.**
  - Current requirements already give board ability to mandate independent chair.
  - No evidence independent chair requirement solves any problem, and in fact, could have negative results.
    - Some fund groups having independent chairs have made headlines for regulatory problems (*e.g.,* Bank of America, Bank One & Putnam).
    - Conversely, many fund groups not having independent chairs such as USAA, Fidelity, Vanguard and T. Rowe Price have not been identified as having regulatory problems.
    - Based on study commissioned by Fidelity, empirical evidence indicates that funds with interested chairs have outperformed funds with independent chairs. In fact, the three highest Lipper awards announced earlier this month went to fund groups having interested chairs: American Funds, Vanguard, and USAA.
    - Chair or CEO of a parent company, like USAA, serving as chair of fund board has interest in promoting a compliance culture to preserve the corporate reputation, and is able to enforce that culture due to supervisory control over the adviser company.

- **Consider alternatives to mandating independent chair requirement.**
  - "Lead" independent director should participate in setting board agenda and chair corporate governance committee; and chair of audit committee should be an independent director.
  - Separate election of chair by both a majority of board and a majority of board's independent directors.

- **Raise minimum percentage of independent directors on mutual fund boards to 66 2/3%, but not 75%.**

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