U.S. Investment Company Corporate Governance Outline
"Lessons from America"

Stuart E. Fross, Partner
Wilmer Cutler Pickering Hale and Dorr LLP
60 State Street
Boston, MA 02109
617-526-6792

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Agenda

1. The Director's Job Description
   A. Current "Best Practices"
   B. Responsibilities of Directors
      i. The Independent Director
      ii. The Management Director

- Some key tasks:
  A. Valuation
  B. Fee Renewal
- Best Practices Lessons from the Market Timing Scandal of 2003

Assumptions

- U.S. “registered” “management” investment companies.
- Investment adviser manages fund under contract.
- Conflicts are fully disclosed in prospectus.
- Shares may or may not be redeemable.
- Two categories
  - “Independent” Directors
  - “Management” Directors

Independent Directors: Best Practices Responsibilities

- Beyond the "Watch Dog"
- November 2003 Letter from SEC Chairman Donaldson to Independent Directors Forum
  - Need to address:
    - i. Management fees
    - ii. Soft dollars
    - iii. Distributor costs paid by shareholders
    - iv. Brokerage arrangements
    - v. Revenue sharing
    - vi. Valuation
    - vii. Conflicts
- Thirty-three specific best practices recommendations

The Independent Directors: Top 10

1. Independent Chairperson
2. Super majority of Independents
3. Separate counsel
4. Ability to hire staff
5. Self selecting
6. Set own compensation
7. Set agenda for meetings
8. Adopt compliance policies and procedures
9. Chief compliance officer: reporting line & compensation
10. Independent Committees: contracts; valuation; and audit.*

Responsibilities of Independent Directors

- The 1940 Act and Rules assign “25” tasks to directors
- 10 Delegated Duties from SEC
- Three examples:
  - Fair value of portfolio securities
  - Approve, continue or terminate advisory distribution and affiliated service provider contracts
  - The “2003 SEC Rules”

U.S. Best Practices – Valuation

- Valuation – Board "owns" fund accounting.
  - (i) Hartland case
  - (ii) Directors censured
- Board Valuation Committee
  - Detailed procedures for valuation
  - New instruments require valuation determination by independent directors
  - Meets to deal with surprises

U.S. Best Practices – Management Fees

- Management Fees – Disclosure is not enough.
  - (i) 1970 Amendments: Fiduciary duty with respect to receipt of advisory fees
  - (ii) Annual renewal process (Gartenberg factors)
    - (a) Nature and quality of service
    - (b) Performance
    - (c) Competitiveness of fees
    - (d) Profit margins

The Management Director

- Independent directors have 33 best practices, 25 regulatory duties and 10 delegated tasks.
- How can non-executive directors do their job?
    i. Part time
    ii. Depend on management for information
- Role of Management Directors:
    i. Duty to inform
    ii. Anything that might be pertinent
    iii. Right to recommend
- Certify financials: CEO/CFO.

Lessons from America: What Management Gets

- Importance of Private Litigation
- Independent directors as “conflicts laundry”
- Potentially more flexibility
- Intrusion associated with independents
- Cost of meetings

What Does the Shareholder Get?

- Potential for “checks and balances”.
- A place to resolve arcane conflicts.
  - When disclosure is not enough
- 2003 Mutual Fund Scandal – tested the utility of U.S. system.
  1. High standard of corporate governance before/higher afterwards
  2. Corporate governance: did it matter at scandal – free firms?
  3. Did corporate governance fail at “scandal firms”?

Lessons From America

1. Independent directors can and do enhance investor protection.
2. Independent directors need management that is open about potential conflicts.
3. Management benefits from comprehensive cooperation with independent directors.