

Welcoming Remarks at the 2007 Investment Company Directors Conference

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Thank you, Bob [Uek]. Good morning and welcome to San Francisco. I am delighted to see all of you at the West Coast version of our annual Directors Conference. As Bob just mentioned, we held the East Coast meeting three weeks ago and received very positive feedback. We have a great program lined up, and I want to express my sincere thanks to all of our speakers.

As part of my welcoming remarks, I would like to provide some context for the sessions you will participate in over the next day and a half. So let me take a step back from the details of our program and examine briefly the guiding principles of fund governance.

The responsibilities of a mutual fund director are rooted in the same time-honored duties of a corporate director. Both types of directors are fiduciaries, and, as such, must meet the duty of care and duty of loyalty. If directors meet these standards, they enjoy the protection of the business judgment rule, which is a judicial doctrine that shields a director from personal liability for decisions made in the boardroom. These important principles must be the framework within which directors—for both operating companies and funds—fulfill their responsibilities and regulators consider governance requirements.

In addition to these general principles, fund directors have specific responsibilities imposed on them by the Investment Company Act of 1940 and by the SEC. The legislative history of the 1940 Act tells us that independent directors were put into place “to supply an independent check on management and to provide a means for the representation of shareholder interests in investment company affairs.”

As overseers, directors should not be involved in a fund’s day-to-day operations. In fact, in 1964, one of the draftsmen of the 1940 Act, Alfred Jaretzki, noted, “If the extent of [the] duties and responsibilities [of fund directors] were pressed to a point where they could be fulfilled only by an expert and require an inordinate amount of time, the choice of non-affiliated directors would be so limited as to curtail even further the availability of

competent persons of broad background.” And, he warned, “the time required in the exercise of their duties would bring the composition of a board very close to a pure management group.”

This insightful observation is more important today than ever before. The principles that guide your oversight require you to review the work of the adviser, to ask questions, and to become comfortable with the process the fund’s service providers follow. They do not demand that you take on the day-to-day responsibilities of managing the fund. In fact, directors who act beyond their role as overseers and take on management-like responsibilities may very well lose the protection of the business judgment rule.

Engaging in management-like functions also could very well set a board up for failure. Derivatives, a panel topic for tomorrow morning, offer a great example of this. While many of you are experts in particular fields, I am not sure that many of you are experts in the complexities of derivatives. Nor should anyone expect you to be. Tomorrow’s panel will focus not on how to become experts in the use of derivatives, but rather on the questions you should ask when the funds you oversee invest in them.

While it is clearly established that the role of directors is to provide effective oversight, not to micro-manage, this distinction is getting more and more difficult to draw as the fund industry grows and its regulatory framework evolves. The SEC often supported new innovations and products developed by the industry through the adoption of rules that exempted funds from certain restrictions of the 1940 Act. These exemptions rely extensively on the oversight capabilities of independent directors.

Undeniably, this process of exemptive relief has contributed to the growth of the industry and the broad range of funds now available to investors. Unfortunately, though, it also has led to director involvement in a number of routine, nondiscretionary items. Board meeting agendas also include items that are not required by rule but rather have become de facto requirements through informal means, such as language in an SEC release. Concern has been expressed that the increased volume of detailed information that directors are asked to consider and, in some instances, evaluate and vote on is preventing them from devoting more time to broader trends and issues affecting funds and their shareholders.

The IDC and the independent director community welcome the initiative that the SEC staff has undertaken to review directors' responsibilities in an effort to determine how the SEC can make directors more effective. As Buddy Donohue will discuss, his objective is to enhance directors' effectiveness, not necessarily to make their jobs easier. Nor was this project initiated in response to a concern about fund board's effectiveness, but rather based on recognition that there is always room for improvement and that there have been significant regulatory and market changes that provide an opportunity to reevaluate current requirements. The guiding principles of fund governance that I described earlier and that have worked to protect the almost 90 million fund shareholders today should provide the framework for this initiative.

Directors, too, must rise to the challenge of effectively fulfilling their fiduciary responsibilities by remaining vigilant in continuing to ask questions of management and probe issues of concern, especially in situations of possible conflicts of interest. Directors also should actively pursue educational offerings, such as this conference, to keep up with regulatory developments and to stay informed of current industry practices. In this regard, I thank each of you for your continued support of the IDC and for your involvement in this important conference. We welcome your suggestions and comments on all aspects of our work on behalf of fund directors.

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And now, turning to the program. We are fortunate to have Buddy Donohue, Director of the SEC's Division of Investment Management, deliver our keynote address. The fund industry and, more importantly, the millions of fund shareholders, benefit greatly by having a Division Director like Buddy, who has years of hands-on experience. Prior to serving at the SEC, Buddy was Global General Counsel for Merrill Lynch Investment Managers. In that position, he oversaw the firm's legal and regulatory compliance functions for over \$500 billion in assets -- including mutual funds, fixed income funds, hedge funds, private equities, managed futures, and exchange funds. Buddy also spent more than a decade as Executive Vice President and General Counsel for OppenheimerFunds.

Please join me in welcoming the SEC's Director of the Division of Investment Management, Buddy Donohue.

