INVESTMENT COMPANY INSTITUTE

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ICI 2003 GENERAL MEMBERSHIP MEETING SPEECHES

[16133] May 30, 2003 TO: BOARD OF GOVERNORS No. 24-03 PRIMARY CONTACTS - MEMBER COMPLEX No. 40-03 SEC RULES MEMBERS No. 66-03 RE: ICI 2003 GENERAL MEMBERSHIP MEETING SPEECHES SEC Division of Investment Management Director Paul F. Roye, Institute Chairman Paul G. Haaga, Jr., and Institute President Matthew P. Fink spoke at the Institute's 2003 General Membership meeting.* Their speeches are summarized below. SEC Division of Investment Management Director Roye's Address Paul Roye's remarks focused on the SEC's efforts to become a proactive regulator and on ways the mutual fund industry could become more proactive for its own benefit and that of its investors. Mr. Roye urged the mutual fund industry to be mindful of the fact that its position in this economy and securities markets is not guaranteed. It must, Mr. Roye said, continually respond to a competitive and changing environment by focusing on the needs and interests of shareholders. Mr. Roye noted that, for its part, the Division of Investment Management has been engaged in "a coordinated effort to identify challenges and high-risk areas within the investment management industry and address them before they become significant investor protection issues." He cited as examples the Division's "integrated reviews" and new proposal relating to compliance programs. According to Mr. Roye, the latter represents an effort to prevent the types of scandals that have plagued other segments of the securities industry from tainting the investment management industry. "These rules do not ask anything that any well- managed fund or adviser should not be doing today," he commented. Mr. Roye indicated that the SEC also is being proactive by targeting its resources in areas that deserve the most attention. Specifically, he mentioned the Office of Compliance Inspections and Examinations' new "risk-based" examinations approach, which results in those complexes found to have weaker controls being examined on a more frequent basis, and the * Paul Roye's speech may be found at http://www.sec.gov. Paul Haaga's and Matthew Fink's speeches may be found at http://www.ici.org/new/03_gmm_haaga_spch.html and http://www.ici.org/new/03_gmm_fink_spch.html, respectively. 2 SEC's fact-finding review of hedge funds, which was intended to identify investor protection issues raised by hedge funds. Mr. Roye urged the mutual fund industry to redouble its efforts to be proactive in identifying and addressing issues and problems that confront the industry and its investors. He noted several areas in which the industry has, in fact, been proactive – providing views on investment companies as investors, addressing market timing issues, issuing best practice recommendations relating to fund governance and personal investing. Noting that some of these initiatives were undertaken to forestall the SEC from imposing harsher requirements, Mr. Roye urged the industry to "take the same kind of proactive approach to other issues, whether or not identified as concerns by regulators, so that the industry can operate in ways that are best for its shareholders -- based on its own insights and

perception of problem areas." In this way, Mr. Roye said, the industry can distinguish itself as one that promotes a fiduciary culture where investor interests come first. Mr. Roye encouraged the industry to adhere to the philosophy that what is good for investors is good for the fund industry. Even where fund companies are not at fault, they may be impacted by a public backlash. Therefore, it is in the industry's best interests to police itself. In contrast to regulators who are one step removed, Mr. Roye reminded the industry that it is "in the best position to question and stop questionable practices before they harm investors and cause a black eye for the industry." Finally, Mr. Roye commented on SEC efforts to examine whether there are better ways to meet the investment needs of fund shareholders. Specifically, the SEC is looking at whether expanded investment strategies should be open to fund investors and Mr. Roye invited industry input on this issue. He also encouraged the industry to continue its efforts at investor education, urging fund companies to identify areas where investors might need additional information as market conditions change. Chairman's Report Paul Haaga opened his remarks by noting that the past year has been filled with great challenges for the nation, the investment company industry and its shareholders. Despite these challenges, Mr. Haaga said, the mutual fund industry has continued to serve investors well. As a result of the industry's ongoing efforts to keep investors educated and informed, most fund investors are not fleeing the market. In addition, the industry has maintained investor confidence by cooperating with regulators and remaining open to new ideas and approaches that benefit mutual fund shareholders. Mr. Haaga addressed recent criticisms of the fund industry. He observed that fund shareholders have benefited from independent scrutiny of mutual funds over the years. Effective criticism has brought a fresh outside perspective to the industry's activities and enforced the highest standards throughout the industry. Benefits to shareholders have included plain-English prospectuses, expanded portfolio holdings disclosure in shareholder reports, more information about on-going expenses in shareholder reports, best practices to strengthen fund governance. 3 However, according to Mr. Haaga, the motivation of some critics lately has not been as clear. "When criticism is unfair, uninformed, or unbalanced, or when critics are motivated more by a desire to sell publications or competing products, or to gain publicity or political advantage, they become too easy for us to ignore and we lose an important opportunity to listen and improve." Mr. Haaga commented that it is important for the industry to stand up for what it believes is in the best interest of shareholders, even if it is not the popular view. He cited the industry's opposition to one part of the proxy disclosure rules – the disclosure of individual votes -- as a recent example. He also mentioned several initiatives the industry has supported in the interest of shareholders, including improvements to the nation's retirement and education savings systems, deferral of taxes on certain capital gains distributions, reforms in the governance of corporate America, reform of the securities markets and broad reforms of the financial services industry. In closing, Mr. Haaga urged the industry to continue to put the best interests of shareholders above all else and to continue to stand up and speak with a united voice before legislators, regulators and the public. He reminded the industry that it must be open to new ideas that will allow it to provide even greater service and benefits to its shareholders. President's Report Matthew Fink echoed Mr. Haaga's sentiment about the difficult times investors have faced over the last few years. Despite the problems, Mr. Fink pointed out that the mutual fund industry has remained relatively free of scandal. He noted that the industry has succeeded because the interests of those who manage mutual funds are well-aligned with the interests of those who invest in mutual funds. Although the industry has enjoyed success, Mr. Fink warned that it should not confuse feeling gratified with being satisfied. The fund industry must assume responsibility for taking meaningful actions to restore investor faith and confidence in the markets. He cited four specific efforts that should guide mutual fund leaders in these efforts: First, the fund industry's support for effective SEC regulation, inspections and enforcement in the interest of investors must be unshakeable. “Popular confidence in mutual funds is built on the effectiveness of the core fiduciary principles set forth in the Investment Company Act of 1940,” Mr. Fink said. “We must never permit these principles to be undermined, diluted, or eclipsed.” Second, mutual fund leaders must actively support regulatory changes that are likely to provide significant benefits to investors. Mr. Fink noted that, in the past 18 months, the industry supported the Sarbanes-Oxley Act and a series of SEC regulatory and disclosure reforms. He indicated that the industry will continue to identify and seek changes in market structure and corporate behavior that will benefit investors. Third, mutual fund leaders must be prepared whenever necessary to help investors by undertaking voluntary measures that go beyond law and regulation. Mr. Fink 4 noted that the Institute currently is working on a compliance paper on side-by-side management of mutual funds and hedge funds, a model code of ethics, and a revised model fund audit committee charter. Fourth, fund leaders must continue helping investors by supporting programs and policies that will assist them in saving for their long-term goals. “We have an obligation to see to it that national policy assists investors,” Mr. Fink said, noting strong fund industry support for a number of pension and tax bills now before Congress. In addition to these guiding principles, Mr. Fink outlined several initiatives and activities the Institute has undertaken to help restore investor confidence. For example, Mr. Fink said, the Institute is supporting a major increase in the SEC’s budget; is working closely with regulators and the brokerage industry to address problems the NASD discovered with breakpoints for fund sales; has called on the Financial Accounting Standards Board to require the expensing of stock options; and is expanding its educational programs for mutual fund directors. Moving forward, Mr. Fink said, the industry will continue to welcome constructive suggestions that will enable it to maintain its tradition of integrity and serving shareholders. It will meet the challenges currently facing the industry and its shareholders by continuing to focus on the best interests of mutual fund shareholders. Marguerite C. Bateman Senior Associate Counsel

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