

MEMO# 18962

June 22, 2005

COURT OF APPEALS RULES IN CHAMBER OF COMMERCE LAWSUIT CHALLENGING FUND GOVERNANCE RULES

©2005 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [18962] June 22, 2005 TO: BOARD OF GOVERNORS No. 30-05 CLOSED-END INVESTMENT COMPANY MEMBERS No. 35-05 SEC RULES MEMBERS No. 80-05 SMALL FUNDS MEMBERS No. 58-05 RE: COURT OF APPEALS RULES IN CHAMBER OF COMMERCE LAWSUIT CHALLENGING FUND GOVERNANCE RULES The United States Court of Appeals for the District of Columbia Circuit today granted in part the U.S. Chamber of Commerce's petition for review of a rule promulgated by the Securities and Exchange Commission requiring that 75% of a mutual fund's directors be independent of the fund's management company and that its chairman be independent.* The Court ruled that the Commission did not exceed its statutory authority in adopting the requirements. It agreed with the Chamber, however, that the Commission failed to adequately consider the costs mutual funds would incur in order to comply with the requirements and failed to adequately consider a proposed alternative to the independent chair requirement. In particular, the Court found that an alternative approach under which each fund would be required to disclose whether it has an interested or an independent chairman, allowing investors to make an informed choice, "was neither frivolous nor out of bounds." Therefore, even though it may ultimately decide that the disclosure approach will not sufficiently serve the interests of shareholders, the Commission was obligated to consider this alternative. The Court remanded the matter to the Commission to address these deficiencies. Frances M. Stadler Deputy Senior Counsel * The Court's order is available at <http://pacer.cadc.uscourts.gov/docs/common/opinions/200506/04-1300a.pdf>. See also Memorandum to Closed-End Investment Company Members No. 59-04, SEC Rules Members No. 125-04 and Small Funds Members No. 97-04 [17952], dated September 3, 2004 (regarding the complaint filed by the Chamber of Commerce).