

MEMO# 15946

April 25, 2003

DRAFT ICI COMMENT LETTER ON NYSE PROPOSAL RELATING TO CORPORATE GOVERNANCE PRACTICES

ACTION REQUESTED [15946] April 25, 2003 TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 30-03 RE: DRAFT ICI COMMENT LETTER ON NYSE PROPOSAL RELATING TO CORPORATE GOVERNANCE PRACTICES As we previously informed you, the Securities and Exchange Commission has published for comment proposed rule changes filed by the New York Stock Exchange relating to corporate governance practices.¹ A draft comment letter on the proposal is attached, and it is summarized below. Comments are due to the SEC by May 8, 2003. We will discuss the draft letter at the Closed-End Investment Company Committee meeting on April 30th. If you are not planning to attend the meeting, please provide me with your comments on the draft letter by that date. I can be reached by email at ddonohue@ici.org, by phone at 202/218-3563, or by fax at 202/326- 5827. General The draft letter states that the Institute's perspectives on the NYSE's proposal are unique in that investment companies are both investors in and issuers of securities. The draft letter states that as investors, the Institute supports the proposal, which will serve to enhance the interests of investors by improving the governance structure of listed companies and the integrity of financial reporting. The letter then provides specific comments on the application of the proposal to investment companies as issuers. The letter preliminarily expresses strong support for the NYSE's determination not to apply many of the proposed requirements to closed-end funds, and none of the proposed amendments to exchange-traded funds. Audit Committee Service on Multiple Audit Committees – The proposal provides that if an audit committee member simultaneously serves on the audit committee of more than three public companies, and the NYSE-listed company does not limit the number of audit committees on which its members can serve, then in each case, the board would be required to determine that such simultaneous service would not impair the ability of such member to effectively serve on the 1 See Memorandum No. 15926, dated April 22, 2003. 2 listed company's audit committee and to disclose such determination in its proxy statement. The draft letter recommends that in applying this requirement to investment companies, the NYSE should treat a "fund complex" as one company in recognition of the fact that it is common practice for the same directors to serve on the audit committee of more than one fund in a complex. In addition, the draft letter notes that fund financial statements are less complicated than the financial statements of operating companies and therefore audit committee oversight requires less time, and that typically all funds in a complex rely on the same accounting system and are subject to the same internal controls and policies. Financial Literacy of Audit Committee Members – The proposal, like the current requirement, would require each member of the audit committee to be financially literate or to become financially literate within a reasonable period of time after appointment to the

audit committee. The draft letter recommends that the proposal be modified to require audit committee members to be financially literate at the time they join the audit committee rather than having these qualifications within a reasonable period of time after the appointment to the committee. The draft letter states that this change should enhance the effectiveness of audit committees and would make the NYSE's requirement more consistent with Nasdaq's recent corporate governance proposal. Review of Earnings Information – The draft letter recommends that investment companies be excluded from the proposed requirement that audit committee members discuss earnings press releases as well as financial information and earnings guidance provided to analysts and rating agencies. The letter states that investment companies do not have earnings targets, nor do they provide earnings guidance to security analysts. The letter also states that such a requirement is not necessary for investment companies because statements of their earnings and their earnings press releases are more straightforward than those of operating companies. Comment Period The draft letter expresses concern with the insufficient amount of time the Commission has provided interested persons to comment on the proposal – i.e., the bare minimum 21-day period. It strongly encourages the Commission to lengthen the comment period for future significant self-regulatory organization rule proposals. Dorothy M. Donohue Associate Counsel Attachment (in .pdf format)