ORAL ARGUMENT SCHEDULED FOR FRIDAY, APRIL 15, 2005

NO. 04-1300

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA,

Petitioner,

v.

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,

Respondent.

Petition for Review of Final Rule of the
United States Securities and Exchange Commission

OPPOSITION OF PETITIONER CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA TO CFA INSTITUTE'S MOTION FOR LEAVE TO FILE AMICUS BRIEF

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A full month after briefing was completed in this case, CFA Institute has submitted a proposed brief *amicus curiae* together with a motion for leave to file the brief. Petitioner U.S. Chamber of Commerce opposes the filing of the brief, which is untimely without good cause, and which is unlikely to aid the Court's decision of the case.

A. The Institute's Motion And Brief Are Untimely.

1. Under this Court's rules, the Institute was required to file a motion to participate as *amicus curiae* "within 60 days of the docketing of the case in this court." Circuit Rule 29(b). The Chamber of Commerce docketed its Petition for Review on September 2, 2004; accordingly, the Institute's motion is nearly 4 months late. The Court's rules provide that a motion to participate as an *amicus* that is filed more than 60 days after the petition is docketed may be granted by the clerk only "as long as the motion is unopposed and as long as the brief will be filed within the time allowed by FRAP 29(e) and this rule." *Id.* Neither condition is met here: The Chamber opposes the motion and, under FRAP 29(e), the Institute's motion and brief would have been due "no later than 7 days after" the SEC's brief was filed on January 12, 2005. The Institute's filing came more than a month after that, when the Chamber already had filed its reply brief. Under this Court's rules, that is prohibited. *See* Circuit Rule 29(c) ("Timely filing") (In the absence of

provision for an *amicus* brief in the scheduling order, "the brief must be filed in accordance with the time limitations described in FRAP 29(e).") (emphasis added).

2. CFA Institute concedes its brief is untimely, but says there is good cause because "unbeknownst to CFA Institute, the briefing schedule for this case was expedited. At the time CFA Institute learned of that fact, certain of its officers required to approve the decision to file this brief were traveling overseas and in no position to address the issue." Motion at 2.

Those weak assertions do not reflect good cause, they reflect insufficient attention to this Court's rules and to the case itself. The briefing schedule in this case is a matter of public record readily ascertainable by anyone. Further, the Chamber's request for expedited briefing, and this Court's decision to grant it, were reported by the press. *See Stay Sought for Mutual-Fund Directors Rule*, WALL ST. J., Sept. 21, 2004, at C3 ("the Chamber of Commerce asked for an expedited hearing on the matter"); Judith Burns, *Court Refuses to Delay Fund Rules*, WALL ST. J., Oct. 19, 2004, at C19 ("the court granted the Chamber's motion for speedy consideration of the case"). Finally, once the Institute learned that it was not in compliance with the Court's rules, it was, of course, incumbent on the organization to recognize the matter as sufficiently important to warrant contacting officers who happened to be overseas. (The Institute has offices on three continents. Motion at 1.)

B. The Institute's Brief Is Unlikely To Aid The Court's Decision.

Rejection of the Institute's brief is appropriate for the additional reason that it fails to provide the support the Institute claims for the two regulatory provisions at issue:

1. During the rulemaking, the Institute opposed both provisions of the rule challenged by the Chamber. The Institute's comments are Exhibit A hereto. (At the time, the Institute was known as the Association for Investment Management and Research. Proposed Br. at 3 n.2.)

With respect to the requirement that the chair of the mutual fund board be independent of the adviser to the fund, the Institute argued that rather than mandate that the chair always be independent, the independent directors should be trusted with the decision to name the chair. "[W]e believe that the independent directors would act in the best interests of shareholders to elect the best-qualified chair, whether or not independent." Ex. A at 2. (The Institute also suggested having a lead independent director. *Id.* at 2-3.) As noted in the Chamber's Opening Brief, the SEC summarily rejected the alterative of having independent directors select the board chair, making the unelaborated assertion that a management chair "serve[s] two masters." *See* Opening Br. at 46-47. It is striking that, while the SEC regarded any management chair as so irretrievably conflicted that no further response to commenters' suggestion was warranted, this was not the view of this

would-be *amicus*, an organization whose "mission" is "to lead the investment profession globally by setting the highest standards of ethics" and which "acknowledges that independence and avoidance of conflict of interest are critical." Proposed Br. at 1-2.

With respect to the requirement that 75 percent of a fund's directors be independent, the Institute advocated a lower two-thirds majority requirement instead; it cogently identified numerous drawbacks to marginalizing the role of management directors in the way the SEC has:

> [I]ndependence alone might not always be in the best interests of the investor if such persons (albeit independent) are carrying out the duties of director while lacking sufficient knowledge or expertise relative to the mutual fund industry. We believe there must be a critical mass of directors who are very familiar with the mutual fund's business model and management, even if these directors are not necessarily independent . . . . [W]e believe it is important that the board should not be asked to compromise its effectiveness so as to insure compliance with a quota mandated by regulation.
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> * * *
>
> In particular, we are concerned that a sufficient pool of qualified candidates may not exist to fully support a 75% supermajority independence requirement. We believe that fund groups and investors alike are best served by board members that bring a wealth of expertise and knowledge to their position.

Ex. A at 2. *Compare* the Chamber's Opening Br. at 13, 15, 46-47.

2. Significantly, CFA Institute's proposed brief characterizes the provisions at issue in this case as regulating mutual fund governance pure and simple. The SEC, knowing that such a characterization undermines the lawfulness

of the rules, argues that the provisions are designed to assure independent oversight of transactions under the amended "exemptive rules." The CFA Institute is more candid: "[T]he SEC has used its rulemaking authority to impose governance rules on investment companies." Proposed Br. at 5. The Institute's brief nowhere mentions the transactions under the exemptive rules that are the supposed target of the rule, instead extolling the rule's value in addressing such general governance matters as "control" of the board "agenda" and the "tone" of board meetings. *Id.* at 8-9. *Compare* the Chamber's Opening Br. at 36-38.

3. CFA Institute also argues that Congress has approved acting as the SEC did here because Congress has not "tak[en] any action" despite the fact the SEC has been asserting similar authority for "decades." Proposed Br. at 5. That argument is factually and legally mistaken.

Most notable, of course, is that Congress did take action: within months of the SEC promulgating the rule, Congress required it to provide "justification" for its independent chair requirement, to conduct further study, to make a report to Congress, and to act on the results of that report. Opening Br. at 23, 39, 43. That hardly constitutes congressional acquiescence in the independent chair requirement, as the Institute implicitly concedes. *See* Proposed Br. at 6 ("Whatever may be inferred from the fact that Congress desired additional information about the independent chair requirement, its failure to require similar

information about the supermajority requirement" suggests approval) (emphasis added).

Further, the Institute is wrong in claiming that the SEC has been issuing rules of this nature for "decades." As explained in the Chamber's Reply, the SEC's exemptive rules historically have regulated transactions under the rules, requiring that they be approved by a majority of independent directors, for instance. In this rulemaking, by contrast, the SEC regulates the board, requiring that for a fund to engage in exempted activities the board must—for all purposes—have an independent chair and 75 percent independent directors. Reply at 1, 18-19.

Finally, the Institute is mistaken in its legal premise regarding congressional acquiescence in interpretations by regulatory agencies. Generally, "Congressional inaction lacks persuasive significance because several equally tenable inferences may be drawn from such inaction. . . ." *United States v. Craft*, 535 U.S. 274, 287 (2002); *Pension Benefit Guaranty Corp. v. LTV Corp.*, 496 U.S. 633, 650 (1990). Accordingly, the Supreme Court's "repeated" "cautions" "against using congressional silence alone to infer approval of an administrative interpretation" apply here. *Schism v. United States*, 316 F.3d 1259,1295-96 (Fed. Cir. 2002). The Institute relies on *Bob Jones University v. United States*, 461 U.S. 574, 600-01 (1983), but in that case Congress's response was deemed significant because in a

12-year period Congress considered and rejected "no fewer than 13 bills" to overturn the IRS interpretation at issue; enacted "numerous other amendments" to the statute during the same period; and held "[e]xhaustive hearings" on the issue. *Id.*[1] There are no such facts here, and it would require far more than congressional silence to confer the broad authority to regulate corporate governance described in the Institute's proposed brief. *Accord SEC v. Sloan*, 436 U.S. 103, 117-18 (1978) (rejecting SEC argument that its statutory interpretation was valid because it had "been both consistent and longstanding, dating from 1944").

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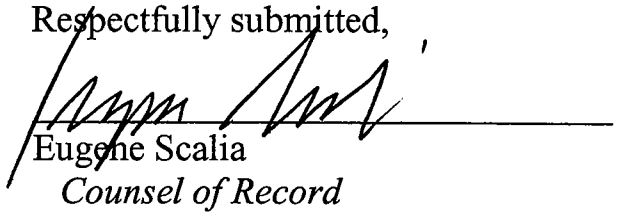
[1] Similarly, in *Eltra Corp. v. Ringer*, 579 F.2d 294 (4th Cir. 1978), cited in Proposed Br. at 5-6, the Court inferred congressional acquiescence not from silence, but from an explicit endorsement in an "exhaustive House Report on" the amended statute, which "declared [the disputed interpretation] be the proper construction." *Eltra Corp.*, 579 F.2d at 297.

CONCLUSION

For the foregoing reasons, CFA Institute's motion for leave to file an *amicus brief* out of time should be denied.

Dated: March 1, 2005

Respectfully submitted,



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CERTIFICATE OF SERVICE

I hereby certify that on this 1st day of March, 2005, I have caused to be served a true and correct copy of Opposition of Petitioner Chamber of Commerce of the United States of America to CFA Institute's Motion for Leave to File Amicus Brief via UPS Next-Day Air, upon the following:

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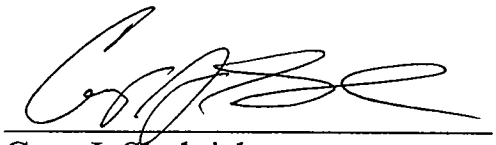

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EXHIBIT A

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19 March 2004

Mr. Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Re: Proposed Rule: Investment Company Governance (File No. S7-03-04)

Dear Mr. Katz:

The U.S. Advocacy Committee (USAC) of the Association for Investment Management and Research (AIMR)[1] appreciates the opportunity to comment on the SEC's proposed rule amendments requiring registered investment companies to adopt certain governance practices.

The USAC is a standing committee of AIMR charged with responding to new regulatory, legislative, and other developments in the United States affecting the investment profession, the practice of investment analysis and management, and the efficiency of financial markets.

Summary Position

We heartily endorse the SEC's focus in this proposal on fund governance practices to strengthen a system that oversees the interests of shareholders in numerous ways. Accordingly, we strongly support the use of a supermajority independence requirement in determining the composition of a mutual fund board. However, we suggest that requiring two-thirds of the board to be independent would be preferable to a 75% requirement.

If the SEC does adopt a supermajority of independent directors standard for mutual fund boards, we do not believe that it is necessary for the chair to be an independent director and would recommend this not be a mandatory requirement. Instead, we recommend that the final rule incorporate the approach of having an independent "lead director".

Finally, we question the usefulness of implementing a new rule requiring directors to do an annual assessment of their performance. We would hope that responsible parties are already performing this assessment, even if informally. We do, however, support the use of mechanisms to remind directors of their ongoing fiduciary duties to shareholders.

These positions are discussed in more detail below.

Discussion

We welcome new procedures and requirements in the mutual fund industry that are designed to address conflicts of interest. We believe there is a compelling need to ensure that investors' best interests remain at the forefront of decision-making while taking into account the complexities of the business world. To this end, we strongly support increasing the number of independent

directors on mutual fund boards, and implementing other measures that can help mitigate the inappropriate influence of self-interested parties.

Board Composition

We strongly endorse the proposition that a fund's board of directors must be "an independent force in [fund] affairs rather than a passive affiliate of management." Since the board serves as the watchdog for investor interests, it must be structured so as to foster independent decision-making and to mitigate potential conflicts of interest. To this end, we support the proposed amendments to require a supermajority of "independent" directors.

We believe that a supermajority of independent directors would go a long way in establishing the appropriate environment within which the board can address business issues that may affect investor interests and to providing a mechanism for making important decisions without undue influence from the fund manager or other interested parties. However, we believe that the goal of fostering objective decision-making can be met with a lower supermajority requirement than the proposed 75%.

In our consideration of this requirement, we strongly agree that a tilt in the board toward independence is desirable. We believe that it will help address some of the issues at the heart of this matter. However, independence alone might not always be in the best interests of the investor if such persons (albeit independent) are carrying out the duties of director while lacking sufficient knowledge or expertise relative to the mutual fund industry. We believe there must be a critical mass of directors who are very familiar with the mutual fund's business model and management, even if these directors are not necessarily independent. Thus, when viewed in its entirety, we believe it is important that the board should not be asked to compromise its effectiveness so as to insure compliance with a quota mandated by regulation.

In particular, we are concerned that a sufficient pool of qualified candidates may not exist to fully support a 75% supermajority independence requirement. We believe that fund groups and investors alike are best served by board members that bring a wealth of expertise and knowledge to their position. Yet, the diverse, specialized or highly technical nature and investment strategy of some funds may require a particular expertise not readily shared by all those who would otherwise qualify for a board position. A number of these specialized funds may fall under the umbrella of a few of the larger fund groups, who could not share directors with the needed expertise, thereby further reducing the pool of qualified board candidates.

In light of this concern, and in our belief that important objectives will not thus be sacrificed, we urge the SEC to reduce the supermajority independence requirement to two-thirds.

Independent Chair

We believe that the supermajority requirement also reduces the need for the board chair to be independent. Instead, we believe that the independent directors would act in the best interests of shareholders to elect the best-qualified chair, whether or not independent.

We appreciate the SEC's concern that there is a heightened possibility of conflicts of interest, when the chair of the fund board is the CEO of the fund adviser. However, when there is a supermajority of independent directors, the chair is unlikely to wield the influence that might occur in a simple majority situation. Moreover, in some situations, we believe that an interested "inside" director may be able to provide experience and insights into complex areas not available from some independent parties. In these situations, having an "interested" person at the helm would ultimately benefit investors' interests.

We therefore endorse the alternative approach discussed in the proposal that would require independent directors to appoint a "lead director" who would be responsible for chairing separate meetings of the independent directors, interacting with their independent legal counsel, and acting as their spokesperson. We believe that such an approach strikes the appropriate

balance for ensuring the continued independence of the board deliberation and decision-making process.

Self-Assessment

Under the proposal, fund directors would be required to perform an annual self-assessment of how well the board and board committees are performing their jobs. In particular, they would be expected to assess the effectiveness of the board's committee structure and whether the directors oversee too many funds.

We believe that these are precisely the types of questions that directors should be asking themselves regularly, not just once a year. In fact, it is arguable that directors who are not engaging in this type of self-assessment should resign their board positions in favor of those who will be more engaged in the type of active debate and critical self-evaluation that comprise a necessary and important part of the director's responsibilities. Thus, we find it tautological that this analysis would have to be mandated by SEC rule.

Conclusion

We strongly support the SEC's efforts, through this rule proposal, to strengthen fund governance structures so that they are more attentive to investor needs. We believe that adopting a supermajority independent requirement alone will go far in appropriately tilting the balance away from conflicted decision-making that may not inure to the ultimate benefit of the shareholder.

If we can provide additional information, please do not hesitate to contact James W. Vitalone at 704.553.0455, jwvitalone@carolina.rr.com or Linda Rittenhouse at 434.951.5333, linda.rittenhouse@aimr.org.

Sincerely,

/s/ James W. Vitalone, CFA

James W. Vitalone, CFA
Chair, U.S. Advocacy Committee

/s/ Linda L. Rittenhouse

Linda L. Rittenhouse
AIMR Advocacy

cc: U.S. Advocacy Committee
Rebecca T. McEnally, Ph.D., CFA - Vice President, AIMR Advocacy

Endnotes

[1] With headquarters in Charlottesville, VA and regional offices in Hong Kong and London, the Association for Investment Management and Research® is a non-profit professional association of more than 69,000 financial analysts, portfolio managers, and other investment professionals in 116 countries of which 56,647 are holders of the Chartered Financial Analyst® (CFA®) designation. AIMR's membership also includes 127 affiliated societies and chapters in 46 countries.