

MEMO# 21896

October 25, 2007

Remarks By SEC's Division Of Investment Management Director At Closed-End Fund Workshop

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TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 37-07 RE: REMARKS BY SEC'S
DIVISION OF INVESTMENT MANAGEMENT DIRECTOR AT CLOSED-END FUND WORKSHOP

The Director of the SEC's Division of Investment Management, Andrew ("Buddy") Donohue, spoke at the Institute's 2007 Closed-End Fund Workshop on October 11th. [\[1\]](#) In his speech, Mr. Donohue focused on valuation issues, issues related to managed distribution plans, and the disclosure regime for closed-end funds. His remarks are summarized below.

Mr. Donohue began by noting his concern that some fund complexes and some fund boards may worry less about the valuation of portfolio securities owned by closed-end funds as compared to those owned by mutual funds. He stated that valuing portfolio securities held by closed-end funds is critically important for several reasons. First, because net asset values ("NAVs") can affect the market prices at which investors purchase and redeem shares in a closed-end fund, it is essential that a closed-end fund's NAV be accurate. Second, NAVs must be calculated correctly to assure that funds pay the correct amount of investment advisory and other asset-based fees. Third, miscalculated NAVs can be materially misleading statements, potentially subjecting the fund, its board and/or managers to liability. Fourth, the Investment Company Act mandates that all funds, including closed-end funds, determine the fair value of a security for which market quotations are unavailable. Mr. Donohue noted that his concerns about accurate valuation have been heightened by recent events in the subprime market and their widespread effect on the broader market.

Mr. Donohue noted the staff's concern that some closed-end funds with managed distribution plans are not sending out the required notices disclosing the sources of the distribution when it is from a source other than net investment income. The staff also is concerned that these notices are only being received by record holders of a closed-end

fund's securities and are not being forwarded to beneficial owners. Further, the staff is concerned that purchasers and potential purchasers of closed-end fund shares may misunderstand, or even possibly be misled about, the nature of a closed-end fund's distributions. In particular, he noted that third-party information providers report "yield" based on a gross distribution that may consist primarily of return of capital. Mr. Donohue also advised fund management and directors to consider whether a current distribution rate is sustainable both at the outset and over the life of the plan.

Finally, Mr. Donohue invited the industry's thoughts and suggestions regarding how the closed-end fund disclosure regime could be improved – whether through interactive data, enhanced use of technology, revised SEC requirements or otherwise.

Dorothy M. Donohue
Senior Associate Counsel

endnotes

[1] His remarks are available on the SEC's website at <http://www.sec.gov/news/speech/2007/spch101107ajd.htm>.

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