

**MEMO# 31710**

April 11, 2019

## **ICI Draft Comment Letter on SEC's Proposed Fund of Funds Rule; Comments due Friday, April 19**

[31710]

April 11, 2019 TO: Closed-End Investment Company Committee  
ETF (Exchange-Traded Funds) Committee  
ETF Advisory Committee  
ICI Securities Regulation Advisory Group  
SEC Rules Committee  
Small Funds Committee  
Unit Investment Trust Committee  
Variable Insurance Products Advisory Committee RE: ICI Draft Comment Letter on SEC's  
Proposed Fund of Funds Rule; Comments due Friday, April 19

In December, the Securities and Exchange Commission proposed a new rule and related amendments under the Investment Company Act of 1940 designed to streamline the regulatory framework for funds that invest in other funds ("fund of funds" arrangements).<sup>[1]</sup> The SEC also is proposing to rescind Rule 12d1-2 under the Investment Company Act and most exemptive orders granting relief from Sections 12(d)(1)(A), (B), (C), and (G) of the Act. Finally, the SEC is proposing related amendments to Rule 12d1-1 under the Act and Form N-CEN.

Although we commend the SEC for its efforts to streamline this complicated framework, the SEC's proposed approach will disrupt a significant number of such arrangements and deprive investors of investment opportunities that have served investors both efficiently and successfully for many years. As a result, we believe that some aspects of the proposed rule must be modified significantly.

ICI has prepared a draft comment letter, which is attached for your review. Please submit comments in writing to [jheinrichs@ici.org](mailto:jheinrichs@ici.org) by Friday, April 19.

In summary, ICI's comments and recommendations include the following:

- *Redemption Restriction.* The proposed restriction on the ability of acquiring funds to redeem shares of acquired funds should be removed from the rule. This restriction is not consistent with the manner in which Congress and the SEC have regulated funds of funds for more than 20 years and would significantly disrupt existing fund of funds

arrangements without any clear justification. Among other issues, the proposed redemption restriction could harm investors in funds of funds by manufacturing artificial liquidity constraints on investments that otherwise offer daily redemptions to all other types of investors. We suggest adopting a regulatory approach similar to the approach that Congress and the SEC have previously taken and that has been successfully serving investors for decades.

- *Other Conditions.* We generally support other proposed conditions to the rule. We believe, however, that some of the requirements relating to the voting of shares of underlying management investment companies should be revised to align with the tested and familiar approach in the current exemptive orders. We also believe that the restrictions on multi-tier arrangements should include additional exceptions.
- *Scope of Proposed Rule.* With respect to the scope of the relief, we support, as proposed, expanding the relief to include all types of registered investment companies and business development companies (“BDCs”) as either acquiring funds or acquired funds. We also believe that the SEC should consider further expanding the scope of the relief to permit private funds and foreign funds to rely on the rule to invest in registered funds or BDCs.
- *Changes to Existing Regulatory Regime.* With respect to the proposal to rescind all orders granting relief from Sections 12(d)(1)(A), (B), (C), and (G) of the Investment Company Act, with the exception of interfund lending orders, we believe that the SEC should clarify that the types of orders that would be rescinded are only those relating to fund of funds arrangements addressed by the proposed rule. Similarly, the SEC indicates that the Division of Investment Management is considering withdrawing all staff interpretive and no-action relief that would be moot, superseded, or otherwise inconsistent with the rule. Given that such guidance and no-action relief are extensive and have been provided over many decades, we believe that the SEC and/or the Division of Investment Management should retain certain letters as discussed below or incorporate the staff interpretive and no-action relief into the rule.
- *Acquired Fund Fees and Expenses.* We recommend that the Commission permit funds to exclude business development companies, or BDCs, from “acquired fund” for purposes of the fee table presentation. This would allow funds to treat BDCs in the same manner as investments in operating companies for expense presentation purposes.
- *Legislative Changes to Address Private Fund Investments in Closed-End Funds.* In conjunction with the rulemaking, we urge the SEC to work with Congress to introduce legislation that prohibits private funds from exceeding the Section 12(d)(1) restrictions when investing in closed-end funds. Contrary to the statutory intent of the section, some private funds are able to exert undue influence over closed-end fund operations to the detriment of long-term shareholders. Amendments to Section 12(d)(1) would limit private fund acquisitions in a manner consistent with the intended goals of the statute.

Our draft letter discusses each of these items in greater detail.

Jane G. Heinrichs  
Associate General Counsel

[Attachment](#)

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