

MEMO# 32991

December 16, 2020

ICI Submits Comment Letter Responding to SEC Staff Questions on Control Share Acquisition Statutes and Enhancing Public Access to Private Markets

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TO: ICI Members

Investment Company Directors SUBJECTS: Closed-End Funds RE: ICI Submits Comment Letter Responding to SEC Staff Questions on Control Share Acquisition Statutes and Enhancing Public Access to Private Markets

Earlier today, ICI submitted the attached comment letter to the Securities and Exchange Commission's Division of Investment Management responding to questions about closed-end funds that relate to state control share acquisition statutes^[1] and retail investor exposure to private offerings.^[2] The letter strongly supports the staff's withdrawal of the *Boulder Total Return, Inc.* no-action letter^[3] and the accompanying staff statement. It is divided into three sections that:

- Respond to questions raised in the staff statement;
- Address certain assertions made in comment letters responding to the staff statement; and
- Respond to certain questions raised regarding the ability of closed-end funds to provide retail investors with exposure to private offerings.

Our letter and the staff statement follow a detailed report ICI submitted to the SEC recommending the withdrawal of the *Boulder* letter and related actions.^[4]

I. Responses to Questions in the Staff Statement

In response to staff questions, the comment letter recommends that the Commission take no further action at this time on the ability of closed-end funds to opt-in to control share statutes. It notes that settled federal judicial precedent already exists in the area that confirms that fund defenses involving voting rights provisions, such as opting into control share statutes, do not violate Section 18(i) of the Investment Company Act. It recommends

that the Commission respect the current judicial precedent and defer to the judicial system to settle ongoing disputes in this area.

The letter states that the ability to opt-in to control share statutes gives closed-end funds and their boards an additional tool to protect fund shareholders when responding to an activist's demands, which often coincide with the activist's self-interested agenda.

In addition, the letter describes some factors that fund directors may consider when determining whether to opt-in to a control share statute. These could involve considering the key policy and purposes of the Investment Company Act, which include mitigating improper influences from affiliates (including activists) that own 5 percent or more of a closed-end fund.

II. Responses to Certain Commenters

The comment letter also responds to several assertions relating to the closed-end fund industry and the procedural and legal aspects relating to the issuance of the staff statement.

Among these, the letter counters assertions that regulated activism benefits all closed-end fund investors and that there are accretive benefits to remaining long-term shareholders when a tender offer is conducted at a price that is below net asset value. It illustrates the harm that long-term shareholders face with certain activist actions, including experiencing fundamental changes to the products that are contrary to what many long-term shareholders sought when making their investment. In addition, it points out that an accretive benefit only occurs once (immediately after the tender offer) and, in the long term, the associated higher fixed costs may erode any possible benefit for remaining investors.

The letter corrects an assertion that leverage, not activism, increases fund expense ratios and counters the assertion that closed-end fund fees should decrease because open-end fund fees have. In addressing these assertions, the letter points to data adjusting for leverage that shows an increase in closed-end fund average total expense ratios immediately following an activist-induced tender offer as compared to similar funds without a tender offer. The letter also highlights the different structures and complexities associated with managing closed-end funds as compared to open-end funds.

It also counters assertions that closed-end funds are unconcerned with the discount levels at which they trade. Here, the letter states that many closed-end funds have tried different strategies to eliminate discounts but that no one mechanism has proven completely effective. Additionally, the letter states that investors buying closed-end funds already are aware of when a fund has a discount and seek closed-end funds for other important investment reasons (e.g., for their investment strategies and yields).

Further, the letter addresses concerns that withdrawing the Boulder letter equates to improper rulemaking and causes ambiguity to the definition of a "voting security" under the Investment Company Act. In so doing, the letter reiterates that the Boulder letter represents a staff statement and is non-binding on the Commission, so withdrawing the letter does not involve a rulemaking or its related procedures. It also states ICI's belief that withdrawing the Boulder letter does not affect whether a share is a "voting security" under the Investment Company Act. It notes that federal courts have found that opting into control share statutes do not render shares to be non-voting securities; rather they only affect the voting rights of certain shareholders.

III. Responses to Staff Questions Relating to Closed-End Funds' Ability to Provide Public Access to Private Markets

The letter reiterates our view that closed-end funds, as regulated funds, can serve as optimal vehicles to provide retail investors with exposure to private market investments. It states that closed-end fund managers, as registered investment advisers, and other fund managers are well positioned to carefully evaluate private market investments and meet certain criteria of sophistication that the SEC has set forth to make such investments. In addition, it adds that any registered closed-end fund structure would be appropriate for retail investors to obtain exposure to the private markets, given that the structures are subject to the Investment Company Act and its many investor protections.

Kenneth Fang
Associate General Counsel

James Duvall
Economist

[Attachment](#)

endnotes

[1] See SEC Division of Investment Management, Control Share Acquisition Statutes (May 27, 2020) (“staff statement”), *available at* www.sec.gov/investment/control-share-acquisition-statutes. The staff statement raised four questions relating to closed-end funds that opt-in to state control share acquisition statutes. A state control share acquisition statute generally restricts the rights of a shareholder who owns more than a certain percentage of a fund’s shares from voting those shares, unless other shareholders restore those rights. For a summary of the staff statement, *please see* ICI Memorandum No. 32487, *available at* www.ici.org/my_ici/memorandum/memo32487.

[2] See Director Dalia Blass, Speech: PLI Investment Management Institute (Jul. 28, 2020), *available at* www.sec.gov/news/speech/blasse-speech-pli-investment-management-institute. Director Blass’ speech raised five questions relating to closed-end funds of private funds and related investor protection concerns. For a summary of the speech, *please see* ICI Memorandum No. 32646, *available at* www.ici.org/my_ici/memorandum/memo32646.

[3] See *Boulder Total Return Fund, Inc.* (pub. avail. Nov. 15, 2010) (“Boulder letter”), *available at* www.sec.gov/divisions/investment/noaction/2010/bouldertotalreturn111510.htm. In the *Boulder* letter, a closed-end fund requested SEC staff input as it considered opting into a state control share statute. In response to the request, the SEC staff determined that opting into the statute would be inconsistent with the requirement in Section 18(i) of the Investment Company Act that every share of stock issued by a fund be “voting stock” and have “equal voting rights” with every other outstanding voting stock.

[4] See ICI, Recommendations Regarding the Availability of Closed-End Fund Takeover Defenses (Mar. 2020), *available at* www.ici.org/pdf/20_ltr_cef.pdf. For a brief summary of the report, *please see* ICI Memorandum No. 32279, *available at*

www.ici.org/my_ici/memorandum/memo32279.

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