

MEMO# 1702

February 5, 1990

CLAIM AGAINST A MUTUAL FUND FOR FAILURE TO DISCLOSE POWER TO LIQUIDATE DISMISSED

February 5, 1990 TO: CLOSED-END FUND MEMBERS NO. 8-90 SEC RULES MEMBERS NO. 12-90 RE: COURT DISMISSES CLAIM AGAINST MUTUAL FUND FOR FAILURE TO DISCLOSE POWER TO LIQUIDATE _____ A case was brought against a mutual fund and certain affiliated parties for alleged violations of various provisions of the federal securities laws and applicable state laws. In summary, the fund had distributed a proxy statement seeking shareholder approval of a change in the fund's investment objective and policies. Approximately six months later, the fund sent a letter to shareholders stating that the board had decided to liquidate the fund. Shortly after receiving the letter, the plaintiffs placed an order to redeem their shares for cash, allegedly at a substantial loss. The United States District Court for the Southern District of New York dismissed the claim brought against the fund under Sections 20(a) and 30(b) of the Investment Company Act of 1940 (the "Act") for failure to disclose in either its proxy or prospectus that the board of directors could liquidate the fund. In dismissing those claims, the court noted that the Complaint did not allege that the defendants omitted information that appeared to be relevant at the time of the issuance of either the proxy or the prospectus. The liquidation was not claimed to have been contemplated and was only alleged to be a speculative possibility. The court stated that a fund cannot be required in proxy statements to address how a power might be used under every possible future circumstance. Moreover, the court held that the fund's documents sufficiently addressed the future possibility of a liquidation in a manner that would be understood by the fund's investors, which the court noted were corporations and "not widows and orphans." With respect to several of the other claims brought against the fund, the court refused to dismiss the plaintiffs' claim under Section 13(a)(3) of the Act, which prohibits a fund from deviating from its investment policy without shareholder approval. The court found that there was a factual issue as to whether the liquidation of the fund was in accordance with the authority granted by the shareholders to temporarily invest the fund's assets in short-term money market instruments. In addition, the court denied the defendants' motion to dismiss the plaintiffs' claim under Section 36(b) of the Act alleging that as of the date the fund began converting its portfolio to cash equivalents, the fund's adviser breached its fiduciary duty by receiving or retaining the fees it was paid. The court's decision was based on the fact that since there had not yet been any discovery, it would be premature to resolve this factual dispute. We will keep you informed of further developments. Amy B. Rosenblum
Assistant General Counsel Attachment

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