

MEMO# 1272

July 18, 1989

NO-ACTION LETTER PERMITTING CLOSED-END FUNDS TO ISSUE PREFERRED STOCK WITH CLASS VOTING RIGHTS

July 18, 1989 TO: CLOSED-END FUND MEMBERS NO. 31-89 RE: NO-ACTION LETTER PERMITTING CLOSED-END FUNDS TO ISSUE PREFERRED STOCK WITH CLASS VOTING RIGHTS _____ The staff of the Division of Investment Management recently granted a no-action request to Drexel Burnham Lambert Incorporated allowing closed-end funds to issue taxable auction rate preferred stock ("TARPS" - a registered service mark) with the voting rights described below. (A copy of the no-action letter is attached.) Drexel licenses the use of its service mark in connection with its participation in underwriting and rendering capital structuring advice to closed-end funds. It is contemplated that the TARPS would be issued by a fund concurrently with the sale of shares of its common stock to provide the fund with investment leverage. The fund also may issue senior notes. The TARPS would have preferred liquidation and dividend rights. Drexel anticipates that the common shares would be offered at \$10 per share and the TARPS at \$100,000 per share. Because of the high minimum purchase price and the fact that the annual dividend rate is reset at periodic auctions, it is expected that the TARPS will be purchased primarily by institutional investors. Each share of common stock is entitled to one vote per share and the TARPS are entitled to either one vote per share or one vote per \$1,000 of liquidation preference i.e., 100 votes per share. A fund's charter would provide that TARPS holders would, as a separate class, elect two directors and the remaining directors would be elected by the common shareholders and the TARPS holders voting together as a class. The TARPS holders and common shareholders would vote as separate classes on amendments to the fund's charter that would adversely effect their respective interests. In addition, TARPS holders and common shareholders would vote as separate classes on various matters such as liquidation, dissolution, merger or consolidation of the fund or a change in the fund's sub-classification as a closed-end investment company, its investment objective or its fundamental policies. - 2 - Section 18(i) of the 1940 Act requires that every share issued by a registered investment company be a voting share and have equal voting rights with every other outstanding voting share. The Commission takes the position that because of the problems with interpreting what constitutes equal voting rights within the meaning of Section 18(i), each individual case must be decided on its particular facts. In its response, the staff noted that it had previously taken a no-action position with respect to a fund that also provided for common and preferred shareholders to vote as separate classes in essentially the same manner as

presented in Drexel's letter. The staff also noted that its no-action position was based, in part, on the fact that TARPS were likely to be purchased by only sophisticated investors. Finally, the staff stated that its response applies only to closed-end funds that issue two classes of securities which are stock. Amy B. Rosenblum Assistant General Counsel
Attachment

Source URL: <https://icinew-stage.ici.org/memo-1272>

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.