

MEMO# 3968

August 3, 1992

SEC PROPOSES RULES TO PERMIT PERIODIC REDEMPTIONS OF INVESTMENT COMPANY SHARES

August 3, 1992 TO: SEC RULES COMMITTEE NO. 52-92 CLOSED-END FUND COMMITTEE NO. 13-92 RE: SEC PROPOSES RULES TO PERMIT PERIODIC REDEMPTIONS OF INVESTMENT COMPANY SHARES _____

The Securities and Exchange Commission has proposed rules and rule amendments to create procedures for the repurchase and redemption of shares of closed-end funds and open-end funds on a periodic basis (e.g., quarterly). Specifically, proposed Rule 23c-3 would provide for periodic repurchases by closed-end funds at net asset value. Proposed Rule 22e-3 would permit open-end funds to effect redemptions less frequently than daily and to extend the payment of redemption proceeds beyond the current 7 day requirement. These proposals would implement the recommendations made in the recently issued report prepared by the Division of Investment Management entitled "Protecting Investors: A Half Century of Investment Company Regulation." A copy of the SEC's release is attached. The proposed changes are consistent with the Institute's recommendation to remove the rigid open-end/closed-end dichotomy so as to permit funds to redeem on a periodic basis, which was submitted in connection with the SEC staff's study of investment company regulation. The significant aspects of the proposals are summarized below.

I. Repurchases By Closed-End Funds

Proposed Rule 23c-3 would permit a closed-end fund to make periodic repurchases under the Rule if it adopted a fundamental policy, changeable only by a shareholder vote, specifying (1) that the company will make repurchase offers and (2) the terms of such offers (which would include the intervals between repurchase offers, the scheduled dates of the repurchase deadlines (i.e., - 2 - the date by which a fund must receive repurchase requests), and the minimum and maximum repurchase amounts). An existing closed-end fund would need a majority vote of its shareholders adopting such a policy in order to begin making periodic repurchases. The Rule would require that repurchase offers be made to all holders of the class of securities to be purchased. A fund could not purchase less than 5% or more than 25% of the shares outstanding. If the amount of shares tendered exceeded the amount offered to be repurchased by the fund, the Rule would require repurchases to be made on a pro rata basis. (However, the Rule provides two options for avoiding this requirement.) The Rule would set forth alternative periodic intervals at which a fund could repurchase its securities. These intervals are 3, 6, 12, 24 or 36 months. A change in the interval would require a shareholder vote. The Rule also would require that repurchase proceeds be paid within seven days after a repurchase deadline. In addition, a fund relying on the Rule would be required to price its shares at least weekly, on a day and at a time determined by its board of directors (which would be required to consist of a majority of independent directors). The proposed Rule also includes a two-part portfolio liquidity

requirement. First, at all times a portion of the fund's portfolio equal to at least 150% of the minimum repurchase amount, as set by the fund, would have to consist of assets that can be sold in the ordinary course of business within 7 business days at approximately the value that the fund uses in valuing its investments. Second, at the time a fund sends out a notification of a repurchase offer, the fund would need assets satisfying the 7 day standard in an amount equal to 150% of the repurchase offer amount. Under the Rule, notification of a repurchase offer would have to be sent to shareholders at least 20 business days before each repurchase deadline and include certain specified information. A copy of the notification would have to be filed with the SEC within 3 business days after it is sent to shareholders. Funds whose repurchase policy provides for the fund to make all repurchase offers for the same amount of securities would be exempt from the notification requirement. The SEC has also proposed a new staff guide to Form N-2 that details the types of prospectus disclosure that closed-end funds making periodic repurchases of their securities would be expected to make. A change to Rule 10b-6 under the Securities Exchange Act of 1934 has been proposed to permit funds making periodic repurchases to continuously offer their shares.

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II. Limited Redemptions By Open-End Funds Proposed Rule 22e-3 would allow a registered open-end fund or registered insurance company separate account, other than a money market fund, to offer redemptions at periodic intervals ("interval funds") or to extend the payment of redemption proceeds beyond the currently required 7 day period ("extended payment funds"). Both types of funds would be able to take up to one month (31 days) to pay redemption proceeds. For interval funds that period would begin with each periodic redemption deadline and the funds would make payment by scheduled redemption payment dates; for extended payment funds the period would begin with the receipt of each redemption request and there would be a rolling deadline for payments. Funds would be required to calculate the net asset value applicable to a redemption request on the next redemption pricing date, which would occur seven days before the redemption payment date. Thus, shareholders who tender their shares for redemption would bear the risk of market changes for the period after they have tendered their shares and before the shares are priced. Disclosure of this risk would be required in the fund's prospectus. For purposes of sales of shares, both types of limited redemption funds would be required to compute net assets value at least daily. Interval funds would be permitted to redeem shares at intervals of 1, 2 or 3 months. Rule 22e-3 would not permit redemptions less frequently than quarterly. Interval fund redemption requests would be revocable until the redemption deadline, but not thereafter. The redemption intervals (for interval funds) and the period between redemption deadlines, pricing dates and payment dates could be changed only upon a shareholder vote. With respect to portfolio liquidity of interval funds and extended payment funds, proposed Rule 22e-3 would require that at least 85% of the assets of the fund satisfy either of two requirements: the fund must reasonably believe that the asset can be sold at approximately the price used in computing the fund's net asset value in a period equal to the fund's period for paying redemption proceeds (the period between an interval fund's redemption deadline and its redemption payment date, or the period between tender and the redemption payment date for an extended payment fund), or the asset must mature before the next redemption payment date. To prevent investor confusion, interval and extended payment funds would be prohibited under Rule 22e-3 from holding themselves out as mutual funds. In addition, a new staff guide to Form N-1A, which focuses on critical areas of disclosure describing a shareholder's rights in a limited redemption

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company, has been proposed.

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III. Comment Period The SEC has solicited comments on a number of aspects of the proposed rules. Comments are due to the SEC 90 days from the date the release is published in the Federal Register.

IV. September 1 Meeting The Institute has scheduled a meeting for September 1, 1992 at 10:00 a.m. to discuss the proposed rules. Please contact Terrye

Rogers at 202/955-3515 by August 19 to let her know whether you will be attending the meeting. Amy B.R. Lancellotta Associate Counsel Attachment

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