

MEMO# 34188

June 21, 2022

ICI Files Amicus Brief Supporting Closed-End Funds' Use of Control Share Provisions

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TO: ICI Members

Investment Company Directors SUBJECTS: Closed-End Funds RE: ICI Files Amicus Brief Supporting Closed-End Funds' Use of Control Share Provisions

Last week, ICI filed the attached amicus curiae ("friend of the court") brief with the United States Court of Appeals for the Second Circuit supporting a closed-end fund's right to use "control share" provisions.[\[1\]](#) The Second Circuit matter arose on appeal after the US District Court for the Southern District of New York held that certain closed-end funds' control share provisions impermissibly violate the Investment Company Act of 1940.[\[2\]](#) Approximately half of the states (e.g., Maryland) have adopted state control share statutes incorporating control share provisions into their laws to protect all shareholders from coercion in proposed tender offers and changes in control. The Second Circuit decision could impact several closed-end funds that have either opted-in to state control share statutes or adopted control share provisions in their governing documents.

Summary of the Brief

ICI's brief urges the Second Circuit to overturn the District Court's decision because:

- The District Court's reading of the Investment Company Act conflicts with the text and purposes of the Act, which aim to protect funds and their shareholders from concentrated shareholders that are affiliated persons of the fund.
- State courts have interpreted parallel provisions to recognize the distinction between voting rights of stockholders and voting rights of stock and have concluded that restrictions on a shareholder's right to vote do not violate the equal voting rights of similar classes of shares.
- The District Court's decision empowers activists to harm closed-end funds and their long-term shareholders. In particular, the brief provides examples in which:
 - Activist strategies have harmed long-term closed-end fund investors; and
 - Appellees' own actions have harmed long-term closed-end fund investors.

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endnotes

[1] A control share provision generally restricts the rights of a shareholder who owns more than a certain percentage of a company's shares from voting those shares, unless the other non-interested shareholders restore those rights.

[2] See *Saba Capital CEF Opportunities 1, LTD v. Nuveen Floating Rate Income Fund*, No. 21-CV-327 (JPO) (D. SDNY filed Feb. 17, 2022) ("opinion"). The District Court decision held that the funds' control share provisions violate Section 18(i) of the Investment Company Act requiring that every share of stock "be a voting stock and have equal voting rights with every other outstanding voting stock." Although "voting stock" is not defined under the Investment Company Act, the court looked principally at the definition of "voting security" under the Act, which is defined as "any security presently entitling the owner or holder thereof to vote for the election of directors of a company." See Section 2(a)(42) of the Investment Company Act. The court reasoned that when a shareholder acquires new stock in one of the funds, and the amount of her stock constitutes a control share, her newly acquired stock does not presently entitle her to vote. Thus, it held that the Investment Company Act renders the funds' control share provisions impermissible. For a summary of the District Court opinion, please see ICI Memorandum No. 34045, available at <https://www.ici.org/memo34045>.

Source URL: <https://icinew-stage.ici.org/memo-34188>

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