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Ms. Dalia O. Blass
Director
Division of Investment Management
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Responses to Staff Questions on Control Share Acquisition Statutes and Retail Investor Exposure to Private Offerings

Dear Ms. Blass:

The Investment Company Institute[1] strongly supports the statement from the staff of the Division of Investment Management concerning control share acquisition statutes ("staff statement") and its simultaneous withdrawal of the *Boulder Total Return, Inc.* no-action letter.[2] Prior to the issuance of the staff statement, we submitted a detailed report strongly recommending the withdrawal of the *Boulder* letter and related actions.[3] We now are writing to respond to questions raised in the staff statement (**Section I**) and certain assertions made in comment letters responding to the staff statement (**Section II**). We also are including responses to certain questions raised in your July speech regarding the ability

[1] The Investment Company Institute ("ICI") is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds ("ETFs"), closed-end funds, and unit investment trusts in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US$25.8 trillion in the United States, serving more than 100 million US shareholders, and US$8.3 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

[2] *See* Division of Investment Management, Staff Statement on Control Share Acquisition Statutes (May 27, 2020), *available at* www.sec.gov/investment/control-share-acquisition-statutes. *See also 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, the SEC staff interpreted the Investment Company Act of 1940 ("Investment Company Act") to prohibit closed-end funds from opting into state control share statutes. State control share statutes restrict the ability of "controlling" shareholders (*e.g.*, those that control more than 10 percent of an issuer's voting securities) from voting their controlling shares, unless the remaining shareholders approve restoring those rights.

[3] *See* ICI, Recommendations Regarding the Availability of Closed-End Fund Takeover Defenses (Mar. 2020) (hereinafter referred to as "report"), *available at* www.ici.org/pdf/20_ltr_cef.pdf.

of closed-end funds to provide retail investors exposure to private offerings while ensuring appropriate investor protections (**Section III**).[4]

I. Responses to the SEC Staff's Questions on Control Share Acquisition Statutes

a. *What are the practical and functional impacts on closed-end funds, their management, and their shareholders when funds opt-in and trigger control share statutes? How are those impacts affected by the availability of other defensive measures? Relatedly, in what circumstances would the availability of other defensive measures affect a fund's decision to opt-in to and trigger a control share statute?*

We do not have any case studies or data at this time on the practical and functional impacts of opting into control share statutes on funds, their management, and their shareholders.

Nevertheless, as we described in detail in our report, 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. In many instances, activists are using their controlling shares to pursue a self-interested agenda to realize the difference in a closed-end fund's market price and its net asset value ("NAV"), demanding that a closed-end fund engage in a liquidity event (*e.g.*, a tender offer, conversion to an open-end fund, or liquidation) so the activist can extract short-term profits. These events can be detrimental to the long-term shareholders who purchase fund shares, not to sell them at NAV or at a price close to NAV, but to benefit from the investment objective and strategies that the fund is pursuing (*e.g.*, exposure to assets not suitable for open-end funds, payments of ongoing distributions).[5] Opting into a control share statute provides an additional tool to address the power of the activist, who is generally an affiliate of the fund by virtue of its holdings.[6]

Allowing boards (including their independent directors), who adhere to fiduciary duties to act in the best interests of the fund, to opt-in to control share statutes allows them to fight the predatory tactics of activists. The more options a board has available to it, the more effective it can be in ensuring that

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[4] *See* Dalia Blass, Director, Division of Investment Management, Securities and Exchange Commission, Speech to the PLI Institute (July 28, 2020), *available at* www.sec.gov/news/speech/blass-speech-pli-investment-management-institute.

[5] For example, the activist's actions may force fundamental changes to the closed-end fund that are contrary to what stockholders sought when making their investment. In addition, activists can demand actions that can cause funds to shrink in size, which may increase costs, or be liquidated altogether, thereby reducing the availability of closed-end funds to investors.

[6] In this regard, opting into control share statutes furthers Congress' stated concern under the Investment Company Act to prevent "affiliated persons" and "investment companies" (among others) from seizing control of funds through concentrated holdings and special voting privileges to further their personal interests. In particular, Congress targeted the use of concentrated voting power to seize control of a fund and pursue self-interested ends, which is detrimental to a fund and its shareholders.

the fund is managed consistent with shareholder expectations. Importantly, opting into a control share statute does not preclude any shareholder proposals or initiatives.[7]

The availability of other anti-takeover defenses would inform a closed-end fund board's decision on whether to opt-in to a control share statute, as boards generally will review their defenses holistically. To the extent that the fund has other available defenses, it could determine how effective the defenses are individually and in tandem at dissuading harmful activist actions. Each defense could be viewed as a tool that the fund can employ to protect itself and shareholders. A board will evaluate its options to determine what tool, if any, to deploy and when. Different tools fit different needs and may be more appropriate to apply in certain scenarios.

b. ***What considerations would a fund's board take into account in determining whether to opt-in to and trigger a control share statute, particularly with regard to benefits to shareholders and compliance with the board's fiduciary duty? Under what specific facts and circumstances would a board decide to opt-in to and trigger a control share statute (or decline to do so)?***

When taking any action, including determining whether to opt-in to and trigger a control share statute, fund directors are guided by their fiduciary duties under state law to act in the best interests of the fund. These fiduciary duties include a duty of loyalty—to exercise powers in the interests of the fund and not in the director's own interest or in the interests of another person or organization; and a duty of care—to exercise diligence in good faith with the care an ordinarily prudent person in a like position would exercise under similar circumstances.[8] Adherence to these duties requires a fund board to carefully weigh the costs and benefits of opting into control share statutes, focusing not on how the action benefits each director, but how it benefits all shareholders of the fund. The board will make these determinations based on all facts and circumstances surrounding the fund, which will include a consideration of the fund's shareholder base, investment objective and strategies, and governing documents.

In particular, a board may consider the key "policy and purposes" of the Investment Company Act, including the need to mitigate any improper influences from its affiliates who own 5 percent or more of

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[7] Shareholders still will be able to engage directly with a fund's board to express concerns and propose steps to address those concerns. Similarly, shareholders could propose alternative board candidates or resolutions for shareholder consideration. If those candidates or proposals are appealing enough to gain the support of the other shareholders, they can be voted into effect. Further, if approved, for some states (*e.g.*, Maryland), the remaining shareholders have the power to restore voting rights to "controlling" shareholders. For more information about the practical and functional impacts that opting into control share statutes may have, please see our report.

[8] *See* American Bar Association – Federal Regulation of Securities Committee, "Fund Director's Guidebook" (4th Ed. 2015).

the fund.[9] As such, in fending off activists, a fund board is well aligned with the most fundamental purposes of the statute. In addition, a board would typically consider the specific circumstances surrounding the fund's existing and anticipated shareholder base and weigh the potential benefits and protections to shareholders of opting into a control share statute against the potential disadvantages and costs. For example, many recently-launched closed-end funds have a finite term upon which the fund will liquidate and redeem shares at the shares' NAV. In these scenarios, a board may determine not to liquidate or open-end the fund in response to an activist proposal to enable its shareholders to continue to receive distributions. A board also may consider the effectiveness of its existing defensive measures and whether additional measures are in the interest of long-term shareholders. It may further consider any related litigation, regulatory guidance, industry trends, shareholder concerns and/or similar facts or circumstances and examine whether they weigh in favor or against opting into the statute in the fund's specific circumstances. Throughout the process, a board typically would be advised by independent director counsel, fund counsel and, sometimes, special local counsel, and would consider the advice and recommendation of other experts.

c. ***Apart from 18(i), which turns on the meaning of "equal voting rights," please explain whether the ability to opt-in to and trigger a control share statute would have a practical or functional impact on a fund's compliance with other provisions of the federal securities***

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[9] The Investment Company Act establishes in its prefatory section that one of its "policy and purposes" is "to mitigate and, so far as is feasible, to eliminate" certain then-existing "conditions" from recurring. 15 U.S.C.A. § 80a-1(b). One of the identified "conditions" to mitigate and/or eliminate is "when investment companies are organized, operated, managed, or their portfolio securities are selected, in the interest of . . . affiliated persons . . . rather than in the interest of all classes of such companies' security holders." *Id.* § 80a-1(b)(2). The Investment Company Act defines an "affiliated person" to include "any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person . . . ." 15 U.S.C.A. § 80a-2(a)(3). In other words, the Investment Company Act expressly provides that one of its key purposes is to prevent investment companies from being run for the benefit of concentrated shareholders and other investment companies, such as activist hedge funds. Thus, to the extent a board has concerns that a particular policy of the Investment Company Act intended to protect fund shareholders is not being furthered, the board may consider taking certain measures to ensure that the policy and purposes of the statute are pursued as intended.

As noted in our report, many activists have exceeded statutory limitations on the percentages of a registered fund's shares that another fund can acquire. In particular, Section 12(d)(1)(A) prohibits a registered or private fund (and any companies the acquiring fund controls) from obtaining more than 3 percent of an acquired registered fund's outstanding voting securities. Section 12(d)(1)(C) prohibits a registered fund, other registered funds having the same the same adviser as the acquiring fund, and any companies the acquiring fund controls, from obtaining more than 10 percent of the outstanding voting securities of an acquired registered closed-end fund. Because the 3 percent limit does not aggregate the holdings of funds controlled by the same adviser, activists have been able to create multiple private funds under common management that each invest up to 3 percent in a targeted closed-end fund, effectively evading the intended limitation on concentrated voting. Likewise, because the 10 percent limit does not apply to private funds, many activists can exceed the limit in a targeted closed-end fund through private funds. *See* report at pp. 7-8. The SEC's new fund-of-funds rule (Rule 12d1-4) imposes restrictions on registered funds investing in closed-end funds but has little impact when investments are made solely through private funds.

> ***laws, such as section 12(d)(1)(E) of the Act, which requires pass-through or mirror voting for certain fund of funds arrangements, or rule 13d-1 under the Securities Exchange Act of 1934, which places a limitation on the ability of certain shareholders from voting based on the size of their holding. If relevant, please provide an analysis of any practical or functional differences between how the principle of equal voting rights may apply in those different regulatory contexts.***

The issue the staff raised in the *Boulder* letter—whether funds can opt-in to control share statutes—involved an interpretive question under Section 18(i) of the Investment Company Act that at least one federal court has already implicitly decided.[10] That court's decisions, which preceded the staff's issuance of the *Boulder* letter, confirm that fund defenses involving voting rights provisions (*e.g.*, implementing poison pills and opting into control share statutes) do not "change the fact that all shares are granted equal voting rights," and thus do not violate Section 18(i).[11] Interpretations under other provisions of the Investment Company Act that may be affected by the withdrawal of the *Boulder* letter generally should revert to how they were interpreted prior to the staff taking the position that it did in the *Boulder* letter.

d. ***Should the staff recommend that the Commission address the ability of a closed-end fund to opt-in and trigger a control share statute in accordance with section 18(i)?***

No. Courts are actively resolving questions related to closed-end funds and control share statutes. We also note that the Commission declined a direct offer by a Maryland district court to submit an amicus brief on these issues in 2007.[12]

Also, as described in our report, the *Boulder* letter was inconsistent with the Investment Company Act and existing federal precedent. Given the settled federal precedent and the current court cases involving certain control share statutes, no further Commission action is necessary or warranted. The Commission should respect the current judicial precedent and defer to the judicial system to settle any ongoing disputes in this area, as it did prior to the staff's issuance of the *Boulder* letter.

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[10] *See Neuberger Berman Real Estate Income Fund Inc. v. Lola Brown Trust,* 342 F. Supp. 2d 371 (D. Md. 2004) ("Neuberger 2004"); *Neuberger Berman Real Estate Income Fund Inc. v. Lola Brown Trust*, 485 F. Supp. 2d 631 (D. Md. 2007) ("Neuberger 2007").

[11] Neuberger 2004, 342 F. Supp. 2d at 376.

[12] Neuberger 2007, 485 F. Supp. 2d 631, at n. 8.

II. Responses to Commenters

As of the date of this letter, the Commission has made public the comment letters responding to the SEC staff's questions on control share statutes. We provide our views below on certain of the assertions in three of those letters.

a. *Comment Letter from Saba Capital (Aug. 14, 2020)*

Saba Capital makes several assertions relating to the closed-end fund industry and the procedural and legal aspects related to the staff statement.[13] We strongly disagree with several of these assertions.

i. Saba Capital's Closed-End Fund Industry Assertions

1. Saba Capital states "[R]egulated fund activism benefits *all* investors"

Saba Capital contends that closed-end fund liquidations and conversions to open-end fund structures enable shareholders trapped in a fund at a persistent discount to exit the fund at NAV. Assuming the shareholder purchased the fund at a discount, the only benefit to a liquidation or "open-end conversion" is the short-term gain. Liquidation and conversions eliminate a shareholder's choice of investment and force fundamental changes to the products that are contrary to what many shareholders sought when making their investment. Saba Capital fails to recognize that long-term shareholders, unlike Saba Capital, have generally not invested in the closed-end fund to realize the difference between the NAV and the market price but have invested for the investment strategy offered by the fund. If such shareholder sought an open-end fund, those are available for investment. Additionally, we understand that Saba Capital's investment exposures may be different than those of long-term shareholders. In some cases, Saba Capital may hedge the investment risk that the closed-end fund is exposed to, so the swing in the closed-end fund's market price is its only investment exposure.[14] And, in the event of a liquidation, as we stated in our report, the distribution from the fund to the shareholder may result in an unexpected tax burden for the year.

Saba Capital also contends that when a fund conducts a tender offer, it is accretive to remaining shareholders because the tender nearly always is priced below NAV, so remaining shareholders get an increase to their NAV that is higher than the increased costs from managing a smaller fund. However,

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[13] *See* Letter from Saba Capital Management, L.P. to Paul G. Cellupica, Deputy Director, Division of Investment Management, SEC, dated Aug. 14, 2020, *available at* www.sec.gov/divisions/investment/control-share-statutes/saba-capital.pdf.

[14] *See*, *e.g.*, Schedule 13D from Saba Capital (Oct. 30, 2020), *available at* www.sec.gov/Archives/edgar/data/1258623/000106299320005267/sched13d.htm ("[Saba Capital] may in the future take such actions with respect to their investment in [a closed-end fund] as they deem appropriate, including, without limitation . . . engaging in short selling of or any hedging or similar transactions with respect to the [shares of the closed-end fund] and/or otherwise changing their intention with respect to any and all matters referred to in Item 4 of Schedule 13D.").

the NAV accretion in this case is only a one-time benefit, and in the long term, the higher fixed costs for remaining investors may chip away at any possible benefit for remaining investors. With less assets to invest, the smaller fund may be less diversified or have less ability to produce attractive levels of income for dividends,.

Additionally, many academic studies spanning decades have discussed the presence and persistence of closed-end fund discounts over time and explore the many different potential reasons for them.[15] As we found in our report, the excess discount for the majority of closed-end funds with tender offers between 2016 and 2018 actually widened to more than they were before the tender offer.[16] In these instances, the value the NAV accretion has on the market price for remaining long-term shareholders is questionable.

2. Saba Capital states leverage, not activism, increased fund expense ratios between 2015 and 2018

In particular, Saba Capital asserts that leverage costs, not activism, were responsible for the increase in the expense ratios of closed-end funds with tender offers in 2017. Leverage costs did play a major role in the rise of total expense ratios for these funds. The average 3-month London Interbank Offered Rate ("LIBOR") was 0.74 percent in 2016 and 1.26 percent in 2017.[17] Many closed-end funds use leverage as a part of their overall strategy, and the sample of funds we presented in our original letter included funds that used leverage. Leverage is often tied to some LIBOR tenor (*e.g.*, 3-month, 12-month), and when borrowing rates rose at the end of 2016 and throughout 2017, the cost for closed-end funds to hold leverage also rose. Because ICI used the total expense ratio from Morningstar Direct, this information was present in our calculation and accounted for a large part of the overall increase.[18]

The data we presented found that the average total expense ratios rose 45 percent for the sample of closed-end funds with activist-induced tender offers in 2017.[19] For these funds, the average leverage ratio was about 35 percent. Using as a sample all closed-end funds with a leverage ratio of at least 35 percent (and excluding those in the original sample), we found that the average total expense ratios rose 34 percent between 2016 and 2017.[20] One likely reason for the difference between the two (the 45 percent increase and the 34 percent increase) is the impact that economies of scale has on fixed costs.

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[15] *See* our report at 51.

[16] *See* our report at 69 (Figure C.13).

[17] Data for the 3-month LIBOR is from the Federal Reserve Bank of St. Louis.

[18] Although information and data provided by independent sources are believed to be reliable, ICI is not responsible for their accuracy, completeness, or timeliness.

[19] *See* our report at 57 (Figure C.6).

[20] This sample represents about 28 percent of all closed-end funds in 2017.

Some fund costs—such as transfer agency fees, accounting and audit fees, and director fees—are relatively fixed in dollar terms, regardless of fund size. After an immediate drop in net assets following a tender offer, these relatively fixed costs make up a larger proportion of a fund's expense ratio, which the remaining long-term shareholders pay. Additionally, some typically stable costs tend to increase in funds that are targeted by activists. These fees may include, among others, printing fees, legal fees, other professional service fees, and additional registration and filing fees, and the fund's shareholders incur these additional costs. It is important to note that Saba Capital asserts that "the increase to NAV to remaining shareholders is often 10 to 20 times greater than the two-cent increase in fixed costs that result from managing a smaller fund." But as we noted earlier, the accretion to the NAV has a questionable effect on the long-term market price of a closed-end fund share, making the long-term impact of additional fixed costs important for shareholders.

3. Saba Capital asserts that closed-end fund advisory fees should decrease because open-end advisory fees have done so

Saba Capital asserts that, because asset-weighted average advisory fees have declined for active and passive mutual funds and ETFs, asset-weighted average advisory fees for closed-end funds should as well. It implies that closed-end fund advisers and boards have refused to pursue or push for lower fees, putting profits ahead of shareholder interests. It also suggests that, because of high advisory fees, if closed-end fund investors switched to actively managed open-end funds, they would save $1.2 billion per year.

We disagree with Saba Capital's premise that, because mutual fund and ETF advisory fees have declined, closed-end fund advisory fees should as well. Many factors influence fees, including a fund's structure, investment objective and strategies, and size.

Closed-end funds are a decidedly different structure and offer investors access to investments and strategies that are different from open-end funds. Notably, a core feature of closed-end funds under the Investment Company Act is that these funds do not offer redeemable securities. Unlike open-end funds, closed-end funds do not need to stand ready to redeem shares and may invest more than 85 percent of assets in illiquid securities, so closed-end funds can invest to a greater degree in less liquid investments, such as private offerings. Because of this, closed-end funds often invest in niche markets with more complex investments. Closed-end funds also may acquire more leverage than the typical open-end fund—they can issue preferred stock and borrow from various sources in addition to the bank borrowings open-end funds can make. Using additional leverage increases the opportunity for enhanced returns but adds another layer of complexity to managing a portfolio. This different regulatory framework under the Investment Company Act is an important overlay to the operation and structure of closed-end funds compared to the operation and management of mutual funds and ETFs under the Investment Company Act.

The size of the average closed-end fund also is important because of economies of scale. The average fund size for closed-end funds was $558 million in total assets at year-end 2019, less than one-third the average fund size for actively managed open-end mutual funds ($1.9 billion in net assets). Additionally, it is more difficult for the assets of a closed-end fund to grow over time—total assets in closed-end funds only grow through returns (which often are distributed as income each year), issuance of preferred share classes, and follow-on offerings. Meanwhile, assets for open-end funds, which are continuously offered as part of the open-end fund structure, will grow as long as investors continue to buy shares of the fund. This is important because some closed-end and open-end funds have management fee breakpoints such that the advisory fee decreases as assets increase. Because of the structural differences, closed-end funds are less able to take advantage of these advisory fee breakpoints.

In addition, fund size is important because smaller closed-end fund managers are less likely to be able to charge a lower advisory fee. Larger complexes have built in economies of scale that allow them to offer their funds with a lower advisory fee. Smaller complexes, on the other hand, tend to need to charge a higher advisory fee to make sure their operating costs are covered so they may continue to operate.

We strongly disagree with Saba Capital's implication that closed-end fund advisers and boards do not push for or pursue lower fees. Closed-end funds are in a highly competitive market,[21] and fund advisers have a strong interest in maintaining low fees. Fund fees and expenses are clearly disclosed to fund investors in closed-end fund prospectuses and now will be required to be disclosed in many closed-end fund annual reports.[22] This information informs an investor's decision on whether to invest in the fund. If fees are too high, then a product may not gain sufficient market interest at the initial public offering or it may not be attractive to long-term investors.[23] Further, as with all regulated funds, closed-end fund boards engage in an annual review of fees in an advisory contract pursuant to Section 15(c) of the Investment Company Act. Boards, including a majority of their independent directors, must approve those advisory fees after receiving all information as may reasonably be necessary to evaluate the terms of the contract, typically including robust comparative information regarding fees, expenses and performance of a fund's peer group and other products managed by the adviser. As with all of their actions, the board must make these determinations pursuant to fiduciary duties to ensure that the action is in the best interests of the fund.

Finally, based on these structural and other differences, we question how Saba Capital can assert that, if closed-end fund investors switched to actively managed open-end funds, they would save $1.2 billion

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[21] *See* ICI, "The Closed-End Fund Market, 2019" at 10, *available at* www.ici.org/pdf/per26-04.pdf. Competitive dynamics have prevented any single sponsor or group of sponsors from dominating the closed-end fund market. For example, in 2019, only eight sponsors offered more than 10 closed-end funds, whereas 40 sponsors offered only one closed-end fund, and 31 sponsors offered two to five closed-end funds.

[22] *See* Securities Offering Reform for Closed-End Funds, Investment Company Act Release No. 33836 (Apr. 8, 2020) ("Closed-End Fund Offering Reform"), *available at* www.sec.gov/rules/final/2020/33-10771.pdf; Instruction 4.h of Item 24 of Form N-2 *See also* Rule 8b-16 under the Investment Company Act.

[23] We note that, when an SEC-registered broker-dealer or investment adviser intermediary recommends a closed-end fund to a retail investor, the recommendation is subject to specified standards of conduct under, as applicable, Regulation Best Interest or an investment adviser's fiduciary duty.

per year. Converting to an open-end fund causes the investment fund structure and the fund's investments to fundamentally change, for example, leading to changes in a fund's underlying investment strategies (*e.g.*, restricting the fund's ability to invest in less liquid assets, use of leverage, managing to meet daily share purchases and redemptions). Saba Capital does not address these differences nor does it explain how it derived the figure. It is most likely that they multiplied closed-end fund assets for 2018 with the asset-weighted average expense ratios for closed-end funds and actively managed mutual funds and ETFs, and took the difference as the cost savings. However, actively managed mutual funds, on average, are much larger than closed-end funds (which gives them much greater economies of scale) and have much more of their net assets in lower-cost strategies (which makes it an inapt comparison). Without this additional information, we believe the statement is quite misleading and, more importantly, fails to account for the investor's decision to choose to invest in a closed-end fund (versus an open-end fund).

4. Saba Capital states "Closed-end fund board members are often paid nearly half a million dollars a year to sit on all the fund boards in a manager's fund complex"

Saba Capital asserts that closed-end fund board members are paid nearly half a million dollars a year to sit on all the fund boards in a manager's fund complex. It asserts that there is no doubt that a board member's interest is more aligned with the adviser than with shareholders.

We believe that the first statement is misleading and strongly disagree with the second. Closed-end fund board compensation is an area left up to each individual board to determine. A fund's board does not take this responsibility lightly. Independent directors typically assess their compensation annually. The time commitment, meeting frequency, complexity of funds served, and other factors may be considered when assessing compensation. Some other important factors, among other things, that determine director compensation include whether the director is the chair of the board, whether the director serves on a committee (or as chair of a committee), and how many meetings the director attends in a given year. In addition, compared to directors that oversee other types of registered funds, directors that oversee closed-end funds often encounter different issues in addition to their oversight of the adviser, because they typically have annual shareholder meetings, comply with exchange listing requirements, and must deal with ever increasing activist activity with the increased probabilities of litigation. Many closed-end fund directors oversee several or all the funds in the complex—including open-end mutual funds and ETFs—to provide consistency and efficiencies, as many issues that affect one fund similarly affect other funds in the complex. Open and closed-end funds must disclose the compensation paid to each independent director annually. Our data shows that the average compensation of a closed-end fund director for all of the funds the director oversees in a fund complex, including open-end funds and ETFs, is approximately $286,000 per year—not even close to the half million dollars that Saba Capital claims is "often" paid.

Furthermore, there is no support for Saba Capital's claim that board members' interests are more aligned with the fund's investment adviser simply as a result of receiving compensation for their board service. Indeed, courts have routinely rejected assertions that board member compensation or service on the boards of multiple funds managed by the same adviser renders a board member *per se* conflicted, interested, or not independent.[24] Indeed, the fund (*i.e*., shareholders) generally pays independent directors' compensation. Thus, the mere fact that board members receive compensation for their service to funds does not suggest that the board members are not acting in the best interests of shareholders, does not undermine the independence of board members, and does not otherwise render board members to be aligned with the adviser.

In short, there is simply no basis for Saba Capital's assertion that directors' interests are more aligned with the adviser than with shareholders. As we discussed above, regardless of compensation, all directors adhere to fiduciary duties to act in the best interest of the fund and must place those interests above their own or anyone else's.

ii. Saba Capital's Procedural and Legal Assertions

1. Saba Capital asserts staff action equates to improper rulemaking

Saba Capital claims that the SEC staff engaged in improper rulemaking when it withdrew the *Boulder* letter. The *Boulder* letter represents a staff statement, not a rule. As recently described by SEC Chairman Clayton, these statements are non-binding on the Commission. He also noted that staff were in the process of reviewing whether prior staff statements should be modified, rescinded or

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[24] *See, e.g.*, *Krantz v. Prudential Invs. Fund Mgmt. LLC*, 77 F. Supp. 2d 559, 563 (D.N.J. 1999) (directors not "interested" in Section 36(b) litigation context merely by virtue of serving on boards of multiple funds and receiving "significant compensation"); *Verkouteren v. Blackrock Fin. Mgmt., Inc.*, 37 F. Supp. 2d 256, 260-61 (S.D.N.Y. 1999) (service on multiple boards for "substantial compensation" is insufficient to overcome presumption that directors are "not controlled" under the ICA); *Kamen v. Kemper Fin. Servs, Inc.*, 939 F.2d 458, 460 (7th Cir. 1991) (similar); *Olesh v. Dreyfus Corp.*, No. CV-94-1664, 1995 WL 500491, at *16 (E.D.N.Y. Aug. 8, 1995) (similar); *Coran v. Thorpe*, 203 A.2d 620, 623 (Del. Ch. 1964) (similar); *Strugala v. Riggio*, 817 F. Supp. 2d 378, 387 (S.D.N.Y. 2011) (receipt of directors fees does not create a conflict of interest for purposes of making demand on board); *Boylan v. Boston Sand & Gravel Co.*, 22 Mass. L. Rptr. 290, 2007 WL 836753, at *10 (Mass. Super. Ct. Mar. 16, 2007) (receipt of "usual and customary director's fees" does not render director interested); *Western Inv., LLC v. Deutsche Multi-Market Inc. Trust*, 34 Mass. L. Rptr. 95, 2017 WL 1103425, at *4 n.5 (Mass. Super. Ct. Feb. 6, 2017) (similar). *See also* ALI Principles of Corporate Governance, § 1.23(a)(3) (1994) ("A director or officer is 'interested' in a transaction or conduct if . . . [t]he director or officer . . . has a material pecuniary interest in the transaction or conduct (*other than* usual and customary directors' fees and benefits) . . . .") (emphasis added); *id.*, Comment ("A director is not interested under § 1.23 solely because the director receives or has an expectation of continuing to receive usual and customary directors' fees, or because a particular transaction in control . . . threatens the loss of the position as a director and therefore of usual and customary directors' fees. Although a usual and customary directors' fee may constitute a significant portion of the annual income of a particular director, that fact alone will not cause the director to be considered interested for purposes of § 1.23 when, as a member of a group of non-management directors, the director considers a transaction in control that could result in the termination of his or her directorship.").

supplemented in light of market or other developments.[25] Accordingly, it was appropriate for the staff of the Division of Investment Management to review the *Boulder* letter and modify, rescind or supplement it.

2. Saba Capital claims staff action creates ambiguity under Section 2(a)(42)

Saba Capital contends that withdrawing the *Boulder* letter would create ambiguity as to what a "voting security" is under Section 2(a)(42), which would pose challenges under other Investment Company Act provisions that use the term.

As we have stated previously, we do not believe that withdrawing the *Boulder* letter affects whether a share is a "voting security" under Section 2(a)(42) for the same reason that it did not implicate the equal voting provision under Section 18(i). Courts have found that actions such as poison pills and opting into control share statutes do not render shares to be non-voting securities; rather they affect the voting rights of the holder.[26] Control share statutes impose restrictions on controlling shareholders, not on the shares themselves. If transferred to a different shareholder not subject to a control share statute, the share can be voted with no issue. Sections 2(a)(42) and 18(i) both concern the voting rights of the shares themselves—the statutory text does not support a conclusion that a limitation on the *holder* has the effect of changing the rights attached to the share itself. Accordingly, issued shares from closed-end funds subject to a control share statute remain "voting securities."

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[25] *See* SEC Chairman Jay Clayton, Statement Regarding SEC Staff Views, (Sept. 13, 2018), *available at* www.sec.gov/news/public-statement/statement-clayton-091318. *See also* 17 C.F.R. § 202.1(d).

[26] *See* Neuberger 2007, 485 F. Supp. 2d 631; *Providence and Worcester Co. v. Baker*, 378 A. 2d 121, 123 (Del. 1977) ("The voting power of the stock in the hands of a large stockholder is not differentiated from all others in its class; it is the personal right of the stockholder to exercise that power that is altered by the size of his holding. In the hands of smaller stockholders, unrestrained in the exercise of their voting rights, the same stock would have voting power equal to all others in the class."). *See also Realty Acquisition Corp. v. Prop Trust of Am.*, Civ. No. JH-89-2503, 1989 WL 214477 (D. Md. Oct. 27, 1989) (holding that a poison pill did not violate a trust declaration requirement that every common share in a real estate investment trust "shall be equal in all respects" to every other common share); *Williams v. Geier*, No. CIV.A. 8456, 1987 WL 11285, at *3-4 (Del. Ch. May 20, 1987) (holding that differentiated voting rights in a corporate charter based on the length of time stockholders held their shares did not violate Delaware's equal voting rights requirement, because the charter did not "provide differing voting rights for the stock, per se"); *Sagusa, Inc. v. Magellan Petroleum Corp.*, No. CIV A 12,977, 1993 WL 512487, at *2 (Del. Ch. Dec. 1, 1993), *aff'd*, 650 A.2d 1306 (Del. 1994) (holding that a "per capita" voting structure, requiring majorities of not only the shares voted but also the stockholders voting, did not violate Delaware's equal voting rights requirement).

b. *Comment Letters from Bulldog Investors (July 28, 2020 and Sept. 13, 2020)*

In two letters,[27] Bulldog Investors asserts, among other things, that:

- restrictions under control share statutes violate Section 18(i) and related provisions under the Investment Company Act that reference "voting securities," voting, or elections;
- the withdrawal of the *Boulder* letter was procedurally improper; and
- the Investment Company Act establishes a fiduciary duty floor for fund insiders.

We have discussed at length our view and judicial precedent that opting into control share statutes is consistent with Section 18(i) and other provisions of the Investment Company Act in our report and in this letter. We also have discussed our views that the staff properly withdrew the *Boulder* letter. Below we address Bulldog Investors' points on fiduciary duties.

Bulldog Investors cites to Sections 36 and 17(h) of the Investment Company Act as imposing federal fiduciary duties on fund directors and officers, and asserts that the Investment Company Act elevates the prevailing fiduciary standards for fund insiders. It claims that the Investment Company Act must establish a nationwide floor for fiduciary duties that supersedes any more "relaxed state law." Related to this, it states that the SEC must provide guidance so that fund directors, trustees, and officers know what is expected when they consider opting into a control share statute.

As a preliminary matter, there is no authority—statutory, case law, or otherwise—that suggests that the Investment Company Act applies an "elevated" standard to a director's fiduciary duties that is more stringent than the standards applied to fiduciaries under state law. Rather, the Investment Company Act provides federal rights of action for very specific conduct, in a manner that parallels rather than supersedes state law. Section 36(a) allows the SEC to bring actions for injunctive relief against directors who have engaged in "personal misconduct" and does not suggest in any way that a new or different standard should be applied to determine whether a breach of fiduciary duty has occurred.[28] Section 36(b) similarly does not ascribe a different standard to be applied when evaluating fiduciary duties, but creates a private right of action against specified entities (not directors) for breaches of fiduciary duties related to the receipt of compensation.[29] Finally, Section 17(h) does not discuss fiduciary duties at all, much less the standard to be applied; rather, the provision identifies specific misconduct—"willful

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[27] *See* Letter from Phillip Goldstein, Managing Member, Bulldog Investors, LLC to The Staff of the Division of Investment Management, dated Sept. 13, 2020, *available at* www.sec.gov/divisions/investment/control-share-statutes/bulldog-investors-091320.pdf; Letter from Phillip Goldstein, Managing Member, Bulldog Investors, LLC to The Staff of the Division of Investment Management, dated July 28, 2020, *available at* www.sec.gov/divisions/investment/control-share-statutes/bulldog-investors.pdf.

[28] *See* 15 U.S.C.A. § 80a-35(a).

[29] *See* 15 U.S.C.A. § 80a-35(b).

malfeasance, bad faith, gross negligence or reckless disregard"—that may not be exculpated by the fund.[30] In short, the Investment Company Act recognizes specific applications of fiduciary duties in the fund context, but nowhere mandates a more stringent standard to be applied to fiduciaries generally.[31]

Closed-end fund directors, trustees and advisers adhere to fiduciary duties and there is ample judicial precedent and guidance on these duties.[32] Fund directors, trustees, officers, and advisers make determinations every day based on their reasonable judgments as to what is in the best interest of fund shareholders. Fund directors will consider the facts and circumstances surrounding a fund and its shareholders when evaluating whether to opt-in to a control share statute. These considered factors will differ from fund to fund and each factor may weigh differently for each fund in the calculus of whether to opt-in to a statute or not. Further courts are continuing to adjudicate issues related to closed-end funds and control share statutes.

c. *Comment Letter from Chris Whitman (Sept. 9, 2020)*

Mr. Whitman asserts that funds are unconcerned with discounts.[33] We disagree. Fund boards and advisers have studied discounts for years and do seek to address them, and closed-end fund boards often receive regular reporting and analysis regarding fund discounts. No entity has identified the precise cause for discounts and even the best performing funds have suffered discounts that enter into the

[30] *See* 15 U.S.C.A. § 17(h).

[31] State laws describe the fiduciary duties that directors follow, which are frequently broader than the specific conduct identified in the Investment Company Act. *See, e.g.,* Mass. Gen. Laws Ann. ch. 156D, § 8.30 (requiring directors to act in good faith, in the best interests of the corporation, and with reasonable care); Md. Code Ann., Corps. & Ass'ns § 2-405.1(c) (requiring directors to act in good faith, in the best interests of the corporation, and with reasonable care); *In re Walt Disney Co. Derivative Litig.,* 906 A.2d 27, 66 (Del. 2006) (recognizing actions taken in bad faith, gross negligence, and "a conscious disregard for one's responsibilities" all constitute breaches of a director's fiduciary duties). State laws also institute limitations on director exculpation. *See, e.g.,* Del. Code Ann. tit. 8, § 102(b)(2)(ii)(7) (prohibiting exculpating directors for, among other things, personal misconduct and acts or omissions not made in good faith); Mass. Gen. Laws Ann. ch. 156D, § 8.51 (limiting director indemnification to actions taken in good faith, in the best interest of the corporation, and in compliance with the law); Md. Code Ann., Cts. & Jud. Proc. § 5-418(a) (prohibiting limitations on director liability for receipt of improper benefits or for "active and deliberate dishonesty").

[32] As described above, many of these fiduciary duties arise from state law. Under the Investment Company Act, Section 36 authorizes the SEC and shareholders of registered funds to bring actions against certain fund insiders for breaches of fiduciary duty in two limited situations. Section 36(a) authorizes actions when a fund director, trustee, officer or adviser engages in personal misconduct. Section 36(b) imposes a fiduciary duty regarding compensation from a fund.

[33] *See* Letter from Chris Whitman to the Division of Investment Management Comment File on Control Share Acquisition Statutes, dated Sept. 9, 2020, *available at* www.sec.gov/investment/control-share-acquisition-statutes-response-20200909-whitman.

double digits.[34] Funds have tried many strategies to eliminate discounts but no one mechanism has proven completely effective. These methods include several of the approaches Mr. Whitman cites, such as implementing share repurchase programs, dividend reimbursement and cash repurchase plans, tender offers, mergers, conversions and liquidations. Other than mergers, conversions and liquidations, which ultimately liquidate a fund in favor of distributing its proceeds at NAV, each of the methods have proven to be effective, if at all, only on a temporary basis with funds often reverting back to excess discount levels that existed prior to the action.[35]

It also is important to note that investors buying closed-end funds are aware when a fund has a discount and seek closed-end funds for other important investment reasons. As described above and in our report, closed-end funds offer strategies and yields that differ and generally are unavailable in an open-end fund,[36] as these two types of funds operate under, at times, different regulatory rules. While Bulldog and other similar investors may be acquiring positions that enable them to pressure management so they can realize the difference between a closed-end fund's market price and its NAV, most retail investors are investing in the fund for other reasons. Among them are a desire to receive higher or more sustainable distributions than might otherwise be available, to invest in a vehicle that is more efficiently invested given that it does not need to meet daily redemptions, and to invest in a fund that can assume a greater amount of leverage. Investors also are attracted to closed-end funds because they are highly regulated and can invest a higher portion of its assets in illiquid, potentially higher yielding investments and asset classes, which is one of the reasons that closed-end funds are not subject to the SEC's liquidity risk management rule (Rule 22e-4 under the Investment Company Act) as are open-end funds.

III. Responses to the Director's Questions about Closed-End Funds Providing Retail Exposure to Private Offerings

Closed-end funds as regulated funds can serve as optimal vehicles to provide retail investors with exposure to private market investments.[37] Regulated funds provide investor protection through a professionally managed investment vehicle with a strong governance framework, subject to

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[34] Although subject to debate, some of the more frequently mentioned factors cited as causing closed-end fund discounts are: market conditions and perceptions; supply of the closed-end funds in a particular market; yield; tax liability; or holding of illiquid securities. ICI, Regulatory Issues for Closed-End Funds (Oct. 2001) at 14-15.

[35] *See, e.g., supra* note 16.

[36] *See*, *e.g.*, Michael Foster, "3 Funds to Buy for $3,400 A Month in Dividends" Forbes.com (Sept. 15, 2020), *available at* www.forbes.com/sites/michaelfoster/2020/09/15/3-funds-to-buy-for-3400-a-month-in-dividends/#3c3b59d02b48.

[37] *See* Letter from Susan Olson, General Counsel, Investment Company Institute, to Vanessa Countryman, Secretary, Securities and Exchange Commission, dated September 24, 2019, *available at* www.sec.gov/comments/s7-08-19/s70819-6190597-192465.pdf.

comprehensive regulation.[38] Closed-end funds, in particular, are not bound by redemption restrictions that impose liquidity and other requirements on their investments. Therefore, unlike mutual funds, they can invest in less liquid assets, like private offerings.

a. ***What criteria would promote access to high quality private market investments? For example, should closed-end funds of private funds invest with fund managers that meet certain experience and scale criteria?***

Closed-end fund managers, as registered investment advisers, as well as investment advisers to any registered funds, are well positioned to carefully evaluate private market investments. These registered advisers will conduct their own due diligence when making these evaluations to ensure that the investments are consistent with the investment criteria set forth in the relevant fund's governing documents and disclosures.

Registered closed-end funds generally qualify as qualified institutional buyers, qualified purchasers, and accredited investors. As with other institutional investors, the SEC appropriately deems regulated funds to have the requisite sophistication to invest in private offerings, and retail investors properly place their trust in fund advisers to make suitable investments. Fund advisers owe fiduciary duties to their shareholders. Those duties ensure that they make investments that are in the best interests of the fund. In addition, fund disclosures already impose restrictions on the investments a fund may make and provide investors with detailed information about those investments.[39]

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[38] The Investment Company Act, among other things, provides important safeguards requiring regulated funds to: confine their use of leverage; restrict their transactions with affiliates; custody their assets with qualified custodians; diversify their holdings; retain fidelity bonds for their officers and employees to protect against larceny and embezzlement; obtain annual audits of their financial statements from independent accountants registered with the Public Company Accounting Oversight Board; and maintain certain books and records. The Investment Company Act also requires regulated funds value their assets pursuant to board-approved valuation procedures and disclose these values, along with their holdings, periodically.

In complying with these provisions, each fund must follow formalized practices pursuant to written policies and procedures reasonably designed to prevent federal securities law violations. Further, regulated funds are required to have a board of directors, which generally have at least a majority of members who are independent of the fund's manager. The board oversees the management, operations and investment performance of the fund and is subject to state law duties of care and loyalty and has specified responsibilities under the Investment Company Act.

The structure and protections offered by regulated funds has no equivalent in the private markets. As a result, a regulated fund can be a helpful tool for providing retail investor access to private offerings with an overlay of governance and regulation.

[39] Regulated funds must provide investors and prospective investors with the fund's prospectus containing key information, in plain English, in a standardized order and format. Many closed-end funds now will be required to reiterate their principal investment strategies disclosure in their annual reports. *See* Closed-End Fund Offering Reform and Rule 8b-16 under the Investment Company Act.

We do not believe that the SEC should require closed-end funds of private funds to invest with fund managers that meet certain experience and scale criteria. The SEC should not impose specific criteria that would disrupt the investment process of registered investment advisers to regulated funds. These managers and regulated funds already are subject to appropriate and comprehensive regulation.

b. ***What closed-end fund structures would be most appropriate for Main Street investors? For example, would an interval fund or tender offer fund provide the right mix of liquidity and access? If so, are there any limitations on an interval fund of private funds strategy given the liquidity requirements in the interval fund rule? Should we consider changes to existing rules to make these funds a more viable option in this context?***

We believe that investments in *any* registered closed-end fund would be appropriate for retail investors, as the Investment Company Act governs all such structures and provides strong investor protections. Each structure offers different investors different advantages. Certain closed-end fund structures, such as exchange-traded closed-end funds and interval funds, may provide liquidity advantages to retail shareholders to allow them to more easily invest in and dispose of their holdings. In this regard, exchange-traded closed-end funds may trade at a discount to NAV but provide daily liquidity through the markets. Interval funds offer less liquidity, but are purchased and sold at NAV. While tender offer funds may limit liquidity for their shareholders, they offer more flexibility to time the receipt of their investment proceeds with a tender offer. Investors or their financial advisers should be the ones choosing the type of vehicle to invest in based on the individual investor's investment objective and risk tolerance. As regulated funds, these funds have fulsome disclosure available for investors and others.

Nevertheless, we believe that the SEC could enhance the interval fund and tender offer fund structures to benefit shareholders. We discussed many of these recommendations in our response to the SEC's concept release on the harmonization of securities offerings.[40]

In particular, we believe that the SEC could provide interval funds more flexibility to conduct their repurchases to offer potentially more periodic repurchases. These recommendations include, permitting interval funds to:

- use flexible intervals from at least one month to up to one year;
- eliminate maximum repurchase amounts;
- conduct more frequent discretionary repurchases;
- modify the elements of a repurchase policy that must be deemed "fundamental;" and
- employ a more efficient notification system.

[40] *See* Letter from Susan Olson, General Counsel, Investment Company Institute, to Vanessa Countryman, Secretary, Securities and Exchange Commission, dated September 24, 2019, at Section IV.b, *available at* www.sec.gov/comments/s7-08-19/s70819-6190597-192465.pdf.

The SEC could allow tender offer funds to reduce costs by meeting filing and notification requirements under the interval fund rule (Rule 23c-3 under the Investment Company Act).

We also are working with our members and broker-dealer intermediaries to improve the order processing functions of interval funds.[41] These improvements, which are outside of the regulatory context, will further facilitate the purchases and sales of interval funds by retail investors.

c. ***Should registered funds limit exposure to private funds that are sponsored or advised by a single adviser? Would allocating assets across multiple advisers promote competition and minimize the risk of unattractive or unsuitable investments? What other risk measures could be put in place by closed-end funds of private funds that would diminish incentives for advisers to take undue risks?***

We do not believe that the SEC should impose restrictions regarding exposure to private funds advised by a single sponsor. As described above, we believe the regulation and duties imposed on registered investment advisers to regulated funds as well as on regulated funds are comprehensive and adequate to protect fund shareholders.

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[41] *See* ICI Operations, *Consider This: Interval Fund Operational Practices* (Sept. 2020), *available at* www.ici.org/pdf/20_ppr_interval_funds.pdf. *See also* ICI Operations, *Interval Funds: Operational Challenges and the Industry's Way Forward* (June 2019), *available at* www.ici.org/pdf/19_ppr_interval_funds.pdf.

ICI and its members appreciate the opportunity to comment on the staff statement on control share acquisition statutes and your questions about the ability of closed-end funds to provide exposure to private offerings. If you have any questions or require any further information, please contact me (202-326-5813), Kenneth Fang, Associate General Counsel (202-371-5430), or James Duvall, Economist (202-326-5908).

Sincerely,

/s/ Susan Olson

Susan Olson
General Counsel

cc: Paul Cellupica, Esq.
Deputy Director and Chief Counsel, Division of Investment Management