VIA ELECTRONIC DELIVERY

May 2, 2019

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Proposed Rule Regarding Fund of Funds Arrangements, Investment Company Act <u>Release No. 33329 (File No. S7-27-18)</u>

Dear Mr. Fields:

Each of the undersigned serves as a Trustee of Advent Claymore Convertible Securities and Income Fund, a closed-end management investment company registered under the Investment Company Act of 1940, as amended (the 1940 Act). We appreciate the opportunity to respond to the request by the Securities and Exchange Commission for comments regarding proposed Rule 12d1-4 under the 1940 Act. As trustees of a closed-end fund we have concerns about fund-of-funds arrangements, particularly when groups of affiliated private funds act in concert to gain excessive influence over closed-end funds. As we discuss below, these actions by private funds seeking to profit from a one-time liquidity event can have an adverse impact on long-term closed-end fund shareholders. In this respect, we concur with the Commission's approach in making Rule 12d1-4 unavailable to private funds. Unfortunately, the parameters the Commission has proposed for reliance on Rule 12d1-4 in order to protect registered funds will not impact the actions of private funds seeking to acquire substantial voting interests in closed-end funds. In our view, additional action by the Commission is necessary in this area in order to fully effectuate the protections Section 12(d)(1)(A)(i) of the 1940 Act was designed to provide closed-end funds and prohibit conduct by private funds that the Commission found necessary to guard against in proposed Rule 12d1-4.

Among the key conditions imposed by the Commission for reliance on Rule 12d1-4 is the requirement that the acquiring fund and its advisory group[1] pass-through voting power to their beneficial owners or "mirror vote" the shares of the acquired fund when they hold in aggregate more than 3% of the voting securities of the acquired fund. In imposing this condition, the Commission clearly found it advisable to protect a registered fund whose shares were being acquired by another fund from the potential undue influence that the acquiring group of funds might achieve over the target registered fund.

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[1] Proposed Rule 12d1-4(d) defines "advisory group" as either "(1) [a]n acquiring fund's investment adviser or depositor, and any person controlling, controlled by, or under common control with such investment adviser or depositor; or (2) [a]n acquiring fund's investment sub-adviser and any person controlling, controlled by, or under common control with such investment sub-adviser."

Unfortunately, private funds today are allowed to operate outside of the intended protections of Section 12(d)(1)(A) and are not subject to the types of conditions proposed by the Commission for reliance on Rule 12d1-4. The 3% limitation in Section 12(d)(1)(A)(i)—which prohibits acquiring more than 3% of a fund's voting securities—is easily avoided because it is applied to a single fund and any company the fund itself controls. Private fund managers are aware of this and circumvent the limitation by causing multiple funds under their control to each invest up to the 3% limit. In this way, private funds, whose actions are coordinated by a common investment adviser (i.e., an advisory group), are allowed to achieve substantial voting interests in registered funds. The adviser is then free to direct the private funds to use their collective voting power to exert undue control or influence over the registered fund. As discussed below, the actions of these private fund advisory groups can be disruptive to the orderly management of a closed-end fund's portfolio and detrimental to the funds and their shareholders.

Once a group of private funds acquires a substantial voting position in a closed-end fund, the adviser of the private funds can take an activist stance and is able to use actual or threatened proxy contests on various proposals to pressure the registered closed-end fund into creating a one-time liquidity event. While an activist group of funds may espouse an intention of taking a stance for operational or management changes, they are often quick to withdraw their proposals if a liquidity event is offered.[2] An often requested liquidity event is a large tender offer. Large tender offers require balancing the benefits of one-time shareholder liquidity and the potential for reduced market price discounts with the impacts of implementing a tender offer, such as the potential for forced sales of less liquid or illiquid securities, realization of taxable gains and the consequences of a fund operating with a smaller pool of assets following the tender.

The reduction in asset size following a tender offer, particularly a large tender offer, can have lasting effects on a closed-end fund. Portfolio management is often impacted. A smaller asset pool may limit a fund's ability to invest in a particular security to the degree desired by a manager and result in increased trading costs. The 1940 Act's asset coverage requirements may also require a fund to reduce its leverage, resulting in lost opportunities for gains or income. Fewer assets also reduce the potential for economies of scale and can result in increased expense ratios as fund expenses are spread over a smaller asset base. Funds shrinking significantly in size may lose analyst coverage, potentially leading to reduced trading volume for their shares in the market. In contrast, if a tender offer is conducted at a price close to the fund's net asset value, the activist funds are able to realize the difference between the discounted market price at which they obtained their shares and the tender offer price, resulting in a quick arbitrage profit without experiencing the potential negative consequences that may follow the tender. Thus, short-term shareholders may be rewarded in a tender offer to the potential detriment of long-term shareholders.

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2 *See* Rose F. DiMartino, *Protecting Closed-End Fund Investors: A Call to Amend 1940 Act Section 12(d)(1)(A)*, The Investment Lawyer, Vol. 26, No. 1 (Jan. 2019).

Other liquidity events sought by activist funds may be more extreme, including the liquidation of the fund or the conversion of the closed-end fund into an open-end structure. These liquidity events can inflict substantial harm on long-term investors in registered closed-end funds. A fund liquidation eliminates a shareholder's chosen investment, and deprives retirees and other shareholders of the consistent revenue streams often offered by closed-end funds. Fund liquidations also reduce competition in the industry. A liquidation may also result in tax consequences for shareholders. Likewise, open-ending the fund would have severe consequences on fund management, including the significantly curtailed ability of open-end funds to use leverage and hold illiquid securities. These changes may impair a formerly closed-end fund's ability to produce income and achieve its objectives. Each of these consequences is detrimental to long-term shareholders and their reliance on the returns and income that closed-end funds are able to provide. Activist fund investors, as noted above, tend not to be long-term shareholders and appear to be content with the potential for the quick arbitrage profit that the liquidation or open-ending provides without apparent concern to the longer-term consequences to the fund.

At the end of 2017, approximately $275 billion was held in over 500 closed-end funds.[3] Many of the investors in closed-end funds are retirees who depend on the steady distributions often provided by closed-end funds.[4] In enacting the 1940 Act, Congress sought to create a structure for investment companies to be managed for the benefit of all shareholders, and to avoid the harms arising when control of investment companies is unduly concentrated through pyramiding of multiple funds.[5] The 3% limitation on investment companies acquiring voting interests of other investment companies embodied by Section 12(d)(1)(A)(i) was intended to help further this purpose. In our view, actions by private funds acting as a group to pursue a one-time liquidity event for short-term gains thwarts this purpose and imperils the ability of closed-end funds to operate efficiently and achieve the investment objective sought by long-term shareholders. As the Commission considers rulemaking in the area of fund-of-funds arrangements, the practice of using multiple individual funds under common control to circumvent the limitations Congress put into place to protect the interests of fund shareholders should be examined and action taken to limit abusive practices.

In light of the concerns expressed above, we encourage the Commission to state in the adopting release for Rule 12d1-4 that it may, pursuant to Section 48(a) of the 1940 Act, disregard technical compliance with the 3% limitation in Section 12(d)(1)(A)(i) and look through to the underlying substance of holdings in situations where the collective voting security ownership of a

3 *See* 2018 Investment Company Institute Fact Book, Chapter 5.

4 *See* Id.

5 *See* Section 1(b) of the 1940 Act.

registered closed-end fund by a private fund advisory group exceeds the 3% limitation and an intent to change or influence the management or control of the registered closed-end fund has been manifested. We believe that such a statement is appropriate and necessary given the above described potential harm to investors in registered closed-end funds, and the Commission's own view that mirror or pass-through voting is a necessary condition of Rule 12d1-4 as a means to protect registered funds from undue influence when acquiring funds exceed the 3% limitation.

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We would be pleased to participate in any direct outreach efforts by the Commission or respond to questions the Commission may have about our comments.

Very truly yours,

/s/ Randall C. Barnes
/s/ Daniel L. Black
/s/ Derek Medina
/s/ Ronald A. Nyberg
/s/ Gerald L. Seizert
/s/ Michael A. Smart

cc: The Honorable Jay Clayton, Chairman
The Honorable Robert J. Jackson Jr., Commissioner
The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner
Dalia Blass, Director, Division of Investment Management