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June 9, 2019

Ms. Vanessa A. Countryman
Acting Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Fund of Funds Arrangements (File No. S7-27-18)

Dear Ms. Countryman:

The term "undue influence" is cited more than 60 times in the referenced release but is not defined. That has allowed many commenters to misuse it as if it means any attempt to change the status quo or control of an investment company. Yet, there is no basis for either of these assertions.[1]

The Commission has previously acknowledged a distinction between proper influence and undue influence.[2] It goes without saying that proper influence should not be impeded. Moreover, it is self-evident that each investment fund is controlled by someone. For the vast majority, that person is the fund's investment adviser.[3] Nothing in the legislative history of the Investment Company Act of 1940 suggests that Congress sought to protect fund managers or directors from a "hostile" challenge by shareholders. Rather, it sought to prevent collusive "sweetheart" arrangements that "were used to enrich the [colluding] individuals at the expense of fund shareholders…."[4]

Consequently, the Commission should foreclose further misuse of the term "undue influence" by adopting the following definition: "Undue influence is an attempt by a large security holder to obtain an economic benefit from an investment company that

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[1] Unfortunately, the proposing release contributes to the problem by occasionally linking the terms "undue influence" and "change of control," e.g., by soliciting comments as to whether there are "other conditions that would better address the risks associated with undue influence or control."

[2] *See* In the Matter of Special Opportunities Fund, Inc. Rel. No. IC- 31213 (August 15, 2014)

[3] *See* Role of Independent Directors of Investment Companies Rel. No. IC-24082 (October 15, 1999) ("Investment advisers typically dominate the funds they advise.")

[4] *See* Proposed Rules to Permit Certain "Fund of Funds" Arrangements Rel. No. IC-26198, (October 3, 2003). ("In some cases, controlling individuals caused the acquired funds to purchase securities in companies in which the individuals had an interest. In other cases, these individuals caused funds to direct underwriting and brokerage business to broker-dealers they controlled-often on terms favorable to the broker-dealer.")

is not shared by all other holders of the same security."[5] For example, if a large shareholder seeks to have the company award a services contract to the shareholder's affiliate, that would constitute undue influence. Conversely, the mere fact that a fund's advisor or its board of directors disagrees with a proposal by a large shareholder creates no inference of undue influence.[6]

"Mirror voting," on the other hand, is well defined as "vot[ing] the shares held by [an acquiring fund] in the same proportion as the vote of all other holders of the acquired fund."[7] However, as we have informed the staff of the Division of Investment Management, an acquiring fund cannot mirror vote its shares of an acquired fund merely by directing its custodian to do so. Here is why that does not work.

Broadridge Financial Solutions, acting as the agent for almost all banks and stock brokers, solicits proxy voting instructions for every shareholder meeting from the beneficial holders of securities of every public company. However, Broadridge has confirmed that it is unable to cause a proxy to be properly mirror voted because, among other reasons, it does not know how shares held by registered shareholders have voted at the meeting (because only the inspector of election has that information). Therefore, if a fund's custodian directs Broadridge to mirror vote a proxy, that will not result in compliance with Section 12(d)(1)(E)(iii)(aa). Instead, an acquiring fund wishing to mirror vote its shares must (1) instruct its custodian to obtain a *legal proxy* from Broadridge, and (2) give that *legal proxy* to the inspector of election prior to or at the applicable shareholder meeting along with the following instructions: "On every matter presented at the meeting, the shares represented by this *legal proxy* are to be voted in the same proportion as the vote of all other shareholders." <u>This is the only way an investment company can comply with the mirror voting option in Section 12(d)(1)(E)(iii)(aa).</u> Therefore, to insure that acquiring funds correctly mirror vote their shares of an acquired fund, the Commission needs to prescribe the foregoing procedure.

Next, on page 57 of the release, the Commission asks: "Does the proposed condition appropriately limit the threat of redemption that an acquiring fund could otherwise use to unduly influence or control an acquired fund?" That is the wrong

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[5] See *In the Matter of Sequoia Partners L.P.*, Investment Company Act Release No. 20644 (Oct. 20, 1994) 57 SEC Docket 2251, ("Section 17(d) of the Act was designed to prevent affiliated persons from exerting undue influence over investment companies by causing them to engage in transactions that confer disparate benefits on such persons.")

[6] <u>See</u> *Regulation of Communications Among Shareholders*, Release No. 34-31326 (Oct. 16, 1992) ("[T]he desirability of a particular initiative subject to a shareholder vote is by its nature judgmental. As to such opinions, there typically is not a 'correct' viewpoint.")

[7] Section 12(d)(1)(E)(iii)(aa) of the Investment Company Act of 1940.

question. Such a threat is very unlikely even if there are no restrictions on redemptions and the release cites no examples of a threat to redeem a large number of shares of an acquired fund in order to exert influence on it.

That is not to say that having to meet an unusually large redemption request is never a problem. But the problem has nothing to do with the motives of the redeeming shareholder, which may be completely benign. Moreover, the problem is not confined to acquiring funds. A large redemption request can come from an individual, a trust, a general investment partnership, a pension fund, an endowment, a bank, an insurance company, an operating company, or a group of individuals and/or pooled entities having a common investment advisor. Thus, the Commission should consider a rule that would allow an investment company to place reasonable limits on any redemption if the board determines that doing so is in the company's best interest. For example, a board might determine that fulfilling a redemption request in excess of 3% of the company's outstanding shares would unduly harm non-redeeming shareholders by requiring the company to sell securities quickly at unfavorable prices. In any event, the problem to be solved should be how to strike a balance between the conflicting interests of redeeming and non-redeeming shareholders.

Lastly, as the release notes, "restricting the ability of funds to determine which acquiring funds may invest in them could have a positive effect on acquired funds' performance, assuming that acquired funds otherwise would block activist investors, who could have a positive effect on acquired funds' governance and operations, and thus have a positive effect on fund performance." Yet, some managers of closed-end funds disagree. They contend that shareholders of closed-end funds need "protection" from "abuse" by activist investors.[8] As of June 7, 2019, according to CEFConnect, only three of 494 closed-end funds had shares that were trading at a discount of more than 20% below NAV.[9] Is it coincidental that each of those three funds has an investment advisor that is unusually hostile to shareholder rights and supports share ownership limitations for activist investors? We think the Commission can connect the dots.

Very truly yours,

Phillip Goldstein
Managing Member

[8] See, e.g., https://www.sec.gov/comments/s7-27-18/s72718-5518736-185187.pdf

[9] See, e.g., https://www.cefconnect.com/closed-end-funds-daily-pricing