Fund Industry Insights

Current Issues Impacting the Registered Fund Industry

October 1, 2021

Seward & Kissel Fund Industry Insights highlights and provides "color commentary" on significant issues, trends and concerns that we see emerging in the industry in response to regulatory initiatives, and other current developments. It primarily addresses issues affecting registered investment companies and exchange-traded funds (funds) under the Investment Company Act of 1940 (1940 Act) and investment advisers registered under the Investment Advisers Act of 1940 (Advisers Act), but also may be of interest to other financial services industry participants.

Mutual Fund to ETF Conversions

On August 11, 2021, J.P. Morgan Asset Management announced its intention to convert four of its mutual funds to exchange-traded funds (ETFs), which is subject to board approval and expected to occur in early 2022.[1] J.P. Morgan's announcement follows the successful mutual fund to ETF conversions undertaken by Guinness Atkinson, Dimensional Fund Advisers and others that were completed earlier this year.

Each of the sponsors that has successfully completed mutual fund to ETF conversions structured the conversions as reorganizations. In general, there are two paths for converting a mutual fund into an ETF or a semi-transparent ETF (ST ETF): direct conversion or reorganization. In a direct conversion, the mutual fund would modify its organizational documents, service provider agreements and registration statement to permit ETF operations. In a reorganization, the mutual fund would reorganize into a new "shell" ETF whose organizational documents, service provider agreements and disclosures contemplate ETF operations. In addition, the "shell" ETF into which the mutual fund reorganizes would have materially the same investment objectives, strategies, policies and restrictions as the mutual fund. We have prepared an outline that summarizes the considerations and steps involved in each of these paths.

Recent SEC Rule Adoptions and Potential Impacts

A. Valuation Rule

On December 3, 2020, the Securities and Exchange Commission (SEC) adopted new Rule 2a-5 under the 1940 Act (Valuation Rule), which addresses valuation practices and the role of the board of directors/trustees with respect to determining the fair value of a fund's investments.

[1] J.P. Morgan Asset Management's announcement is available here: https://www.prnewswire.com/news-releases/jp-morgan-asset-management-proposes-conversion-of-select-mutual-funds-to-etfs-301353013.html.

The Valuation Rule defines the term "readily available market quotations" for purposes of when a security is required to be fair valued and all other purposes under the 1940 Act and rules thereunder, including Rule 17a-7. Because the definition of "readily available market quotations" under the Valuation Rule would exclude securities that are valued using level 2 and level 3 inputs under the U.S. Generally Accepted Accounting Principles (GAAP) fair value hierarchy, it conflicts with prior SEC Division of Investment Management (IM) staff (Staff) interpretative guidance under Rule 17a-7 that permitted cross trades of certain types of fixed income securities (which are valued using level 2 inputs as defined by GAAP) between affiliated funds. The SEC recognized in the release adopting the Valuation Rule that this new definition would be disruptive to current industry practices, and indicated that both changes to Rule 17a-7 and withdrawal or modification of prior Staff guidance were under consideration.

The compliance date for the Valuation Rule is September 8, 2022. Compliance with the definition of "readily available market quotations" for purposes of effecting cross trades under Rule 17a-7 is not required until that date. The Staff confirmed in an FAQ that a fund could voluntarily comply with the Valuation Rule prior to the compliance date without complying with the new definition of "readily available market quotations" for cross trades undertaken in reliance on Rule 17a-7 until the compliance date.[2] On March 11, 2021, the Staff issued a statement and request for comments on the following areas as it evaluates updating Rule 17a-7 and changes to existing Staff letters interpreting Rule 17a-7:

- current cross trading practices;
- pricing and liquidity;
- cross trading systems;
- compliance controls;
- public reporting of cross trade information; and
- potential costs and benefits of cross trades.

Amendments to Rule 17a-7 are currently on the SEC's rulemaking agenda.[3]

In response to the Staff's request, the Investment Company Institute (ICI) submitted a comment letter (ICI Comment Letter), which provided supporting data on the current benefits of Rule 17a-7 cross trades with respect to fixed income securities and proposed modifications for the rule.[4]

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[2] *See Valuation Frequently Asked Questions* (Updated March 18, 2021), *available at:* https://www.sec.gov/investment/valuation-faq.

[3] The SEC's rulemaking list on the Office of Information and Regulatory Affairs' Spring 2021 Unified Agenda of Regulatory and Deregulatory Action is available here: https://www.reginfo.gov/public/do/eAgendaMain?operation=OPERATION_GET_AGENCY_RULE_LIST¤tPub=true&agencyCode=&showStage=active&agencyCd=3235&csrf_token=7CE97CC2D49C9B6B70868F7B2752E582C86F1945A4A46F34426C18AF1ABE101E611318F64B67159C3A36E7556BD0FB872C8F (SEC Rulemaking Agenda).

[4] *Letter from Susan Olson, ICI, to Sarah ten Siethoff, Acting Director, SEC re: Staff Statement on Investment Company Cross Trading* (Apr. 9, 2021).

The ICI Comment Letter estimated that cross trading of fixed income securities saved funds approximately $329 million in transaction costs in 2020. Advisers' clients generally, exclusive of funds, were estimated to receive benefits of more than approximately $61 million in 2020 from cross trades involving funds in compliance with Rule 17a-7. The ICI proposed that amendments to Rule 17a-7 permit cross trading of level 1 and level 2 securities under GAAP and incorporate modifications to the rule's conditions that: (i) update the pricing provision to require that the price of any cross trade be valued consistently with a fund's Rule 17a-7 and valuation policies and procedures and the adviser's duty of best execution and loyalty; (ii) require risk management policies and procedures tailored to the particular types of securities eligible for cross trading; (iii) revise existing board approval and reporting requirements to incorporate recent no-action guidance that permits the board to rely on quarterly certifications from the fund's chief compliance officer, instead of approving transactions after the fact, and provide enhanced board reporting; and (iv) require more detailed reporting to the SEC on cross trades made in reliance on Rule 17a-7.

S&K Observations/Insights: The condition of Rule 17a-7 requiring securities to have "readily available market quotations" is not mandated by the text of the 1940 Act. The SEC included this condition for policy reasons to provide a basis for considering a cross trade effected in reliance on its conditions to be fair and reasonable to each fund and not involve overreaching.[5] The ICI Comment Letter argues that the SEC's prior amendments to Rule 17a-7 permitting crosses of certain non-exchange-traded securities (subject to alternative pricing conditions) contemplated that certain fixed-income securities, such as municipal securities, Government securities and money market instruments, could be eligible for crossing under Rule 17a-7 provided that the pricing condition could be satisfied. Arguably, a fixed income security that is traded between funds advised by the same adviser that is valued consistently using level 2 inputs would not present overreaching concerns with respect to price, assuming both funds use the same methodology to value the security before and after the trade. Other commenters in response to the Staff's statement and request for comments have suggested that additional liquidity criteria could be added to the rule to address other possibilities of overreaching (*e.g.*, one fund selling fixed income securities to another fund in order to exit a position that has become illiquid).[6]

B. *Derivatives Rule*

Section 18 of the 1940 Act generally limits a fund's ability to obtain leverage or incur obligations through the issuance of "senior securities." A "senior security" is defined, in part, as "any bond, debenture, note, or similar obligation or instrument constituting a security and evidencing indebtedness." The definition of

[5] *See Exemption of Certain Purchase or Sale Transactions Between a Registered Investment Company and Certain Affiliated Persons Thereof,* SEC Rel. No. IC-11676 (March 10, 1981), 46 Fed. Reg. 17011, 17013 ("By limiting the purchases or sales authorized under rule 17a-7 to securities for which market quotations are readily available and requiring the transactions to be effected at the independent current market price for such security, the Commission believes the potential for abuse would be remote. Reliance upon such market quotations provides an independent basis for determining that the terms of the transaction are fair and reasonable to each participating investment company and do not involve overreaching.").

[6] *See* Jack W. Murphy Comment Letter re: Staff Statement on Investment Company Cross Trading at 2, 5 (May 6, 2021), *available at:* https://www.sec.gov/files/jack-murphy.pdf and SIFMA AMG Comment Letter re: Rule 17a-7 Rulemaking at n. 20 (Apr. 12, 2021), *available at:* https://www.sec.gov/files/securities-industry-financial-markets-association-asset-management-group.pdf.

"senior security" in Section 18(g) also includes "any stock of a class having priority over any other class as to the distribution of assets or payment of dividends" and excludes certain limited temporary borrowings.

Rule 18f-4 under the 1940 Act, which was adopted by the SEC in November 2020, provides an exemption from these limitations with respect to the issuance of senior securities that may be deemed to arise when a fund uses certain types of derivatives and engages in other transactions that involve leverage without the use of bank borrowings or the issuance of senior classes of equity securities. Rule 18f-4 supersedes the guidance provided by the SEC in an interpretive release, Securities Trading Practices of Registered Investment Companies, SEC Rel. No. IC-10666 (Apr. 18, 1979) (Release 10666), as well as the guidance provided by the Staff through various no-action letters concerning a fund's use of derivatives and financial commitment transactions since Release 10666 was issued, with respect to the Section 18 concerns addressed by the rule.

A fund that is not a "limited derivatives user" (as defined in Rule 18f-4)[7] is required to adopt a derivatives risk management program (DRMP), designate a derivatives risk manager (DRM) that is approved by the board and comply with either an absolute or relative value-at-risk (VaR)[8] limitation, which establishes an outer limit on fund leverage risk. The VaR limitation limits a fund to 200% of the VaR of a designated reference portfolio (which limit is increased to 250% for closed-end funds) under the relative VaR test, or 20% of the fund's NAV (25% for closed-end funds) under the absolute VaR test, if the DRM reasonably determines that a designated reference portfolio would not provide an appropriate reference for purposes of the relative VaR test.

Rule 18f-4 became effective on February 19, 2021, and the compliance date for the rule is August 19, 2022, which is when prior asset segregation guidance issued by the SEC and its Staff under Section 18 will be rescinded.

S&K Observations/Insights: Prior to the compliance date of Rule 18f-4, funds that engage in "derivatives transactions" (as defined in the rule) and which cannot qualify as a "limited derivatives user" will need to adopt a DRMP and designate one or more natural persons as the DRM that are approved by the fund's board. The rule requires one or more officers of the adviser to serve in this role, but the board cannot appoint the adviser as an entity or designate a committee created by the adviser to serve in this role. (The rule also prohibits the DRM position from being filled by a fund's portfolio manager, if a single person serves in this position.)

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[7] A fund can qualify as a "limited derivatives user" under Rule 18f-4 if: (i) the fund adopts and implements written policies and procedures reasonably designed to manage the fund's derivatives risk; and (ii) the fund's derivative exposure does not exceed 10% of the fund's net asset value (NAV), calculated as prescribed in the rule.

[8] VaR is an estimate of a portfolio's potential losses over a given time horizon and at a specified confidence level.

The adoption of Rule 18f-4 presents opportunities for advisers to employ additional strategies in a fund vehicle. When the SEC adopted Rule 18f-4, the SEC also adopted amendments that permit inverse and leveraged ETFs to rely on Rule 6c-11 (ETF rule). Certain fund sponsors have already launched new leveraged and inverse ETFs, which would also be affected by Rule 18f-4's limitations that may restrict exposures to an underlying index to less than 200%. Other strategies that use short selling or derivatives that were previously limited by the prior asset segregation guidance may be permissible under Rule 18f-4, provided that they can comply with the applicable VaR test.

Regulatory Developments Concerning Environmental, Social and Corporate Governance (ESG) Strategies

The current version of the SEC's rulemaking agenda includes an item for proposing requirements for funds and advisers on the use of ESG factors, including ESG claims and related disclosures.[9] The SEC previously issued a request for comment in March 2020 on current requirements that restrict the use of potentially misleading fund names (principally, Rule 35d-1 under the 1940 Act (Names Rule)).[10] That release highlighted challenges that the Names Rule poses for funds with investment mandates that include criteria that require some degree of qualitative assessment, such as ESG investment mandates. The release also requested comment on such questions as whether the Names Rule should apply to funds that use terms such as "ESG," "sustainable," "tax managed" or "short term" in their names, and whether alternative approaches to regulate fund names should be used. The request sought feedback on whether current requirements are effective and whether there are viable alternatives that the SEC should consider.

Recent statements by Commissioners Peirce and Crenshaw suggest that the Commissioners do not agree as to how the SEC should proceed with ESG disclosure recommendations.[11] In her remarks at the July 7, 2021 Asset Management Advisory Committee (AMAC) meeting, Commissioner Peirce questioned whether ESG metrics could be as objective and comparable across issuers as financial reporting standards are for issuers that file financial statements under the Securities Exchange Act of 1934 (1934 Act). Commissioner Crenshaw's prepared remarks at that meeting indicated that the SEC's purpose should be to "ensure that ESG-related disclosures are consistent, comparable, high-quality, and decision-useful."

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9 *See* SEC Rulemaking Agenda, *supra* note 3.

10 *Request for Comments on Fund Names,* SEC Rel. No. IC-33809 (Mar. 2, 2020), *available at:* https://www.sec.gov/rules/other/2020/ic-33809.pdf.

11 *See* Commissioner Hester M. Peirce Remarks at Asset Management Advisory Committee Meeting (Jul. 7, 2021), *available at:* https://www.sec.gov/news/public-statement/peirce-amac-remarks-070721 and Commissioner Caroline A. Crenshaw Remarks at Asset Management Advisory Committee Meeting (Jul. 7, 2021), *available at:* https://www.sec.gov/news/public-statement/crenshaw-amac-remarks-070721.

In testimony before the United States Senate Committee on Banking, Housing, and Urban Affairs on September 14, 2021,[12] Chairman Gensler reiterated the SEC's commitment to promulgate new ESG disclosure rules, including those related to climate change and human capital. In addition, he referenced the growing number of funds that market themselves with terms such as "green" or "sustainable" and indicated he asked the Staff to consider ways to determine what information stands behind such claims and how the SEC can ensure that the public has the information it needs to understand the investment choices among these types of funds. And in previous remarks made before the European Parliament Committee on Economic and Monetary Affairs on September 1, 2021,[13] Chairman Gensler specifically stated he had directed the Staff to review current practices and consider recommendations about whether such funds should disclose the criteria and underlying data they use to market themselves with terms such as "green" or "sustainable."

S&K Observations/Insights: After the comment period ended on the Names Rule release on May 5, 2020, we understand that the Staff subsequently informally took the position in the context of reviewing fund registration statements that the Names Rule applies to ESG terms used in a fund's name, which would generally require a fund to define what is meant by these terms with respect to the types of investments the fund makes and to invest at least 80% of its assets in those types of investments. Whether a particular name is subject to Rule 35d-1, unless it falls within four broadly defined categories specified in the rule (such as names tied to a particular industry or in a certain country or geographic region), has historically been informed by commentary in Rule 35d-1's adopting release and interpretative guidance provided by the Staff.[14] The proposed rulemaking may seek to add ESG criteria to these categories within the rule.

What is unique about this rulemaking is that the SEC Rulemaking Agenda includes proposals relating to issuers' disclosures about climate change risks and opportunities and human capital management, which raises the question of whether the requirements imposed on funds and advisers that pursue ESG strategies will be complementary to that rulemaking. If climate change and human capital management-related disclosures among companies are standardized, however, there may still be discrepancies in how different issuers interpret and/or apply disclosure requirements, which will introduce elements of judgment and subjectivity in an adviser's utilization of such data and subjective elements into its ESG evaluations. This may make compliance with new ESG disclosure requirements for funds and advisers more complex to the extent that they are tied to new public company disclosure requirements.

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[12] *See* Chairman Gensler Remarks at Testimony Before the United States Senate Committee on Banking, Housing, and Urban Affairs (Sept. 14, 2021), *available at:* https://www.sec.gov/news/testimony/gensler-2021-09-14.

[13] *See* Chairman Gensler Remarks at Remarks before the European Parliament Committee on Economic and Monetary Affairs (Sept. 1, 2021), *available at:* https://www.sec.gov/news/speech/gensler-remarks-european-parliament-090121.

[14] *Frequently Asked Questions about Rule 35d-1 (Investment Company Names)*, *available at:* https://www.sec.gov/divisions/investment/guidance/rule35d-1faq.htm.

Other Rulemaking Contemplated by the SEC Rulemaking Agenda

Other rulemaking contemplated by the SEC Rulemaking Agenda includes rules relating to: (i) certain third party service providers such as index and model providers; (ii) amendments to custody rules for registered investment advisers; (iii) amendments to Form PF; (iv) money market fund reforms; (v) open-end fund liquidity and dilution management; and (vi) shareholder reports, annual prospectus updates and fund advertisements.

S&K Observations/Insights: Future rulemaking with respect to index providers may seek to address an issue highlighted in a recent settled enforcement action involving an index provider for an exchange-traded note (ETN). On May 17, 2021, the SEC announced a settlement agreement with S&P Dow Jones Indices LLC, which published and calculated the index for an ETN tied to S&P 500® Index volatility, relating to alleged violations of Section 17(a)(3) of the Securities Act of 1933 (1933 Act) due to an undisclosed "auto hold" feature that occasionally stopped real-time updates to the published intraday index values and prevented investors from ascertaining that the ETN was in danger of being repurchased by the issuer during an unprecedented spike in volatility on February 5, 2018.[15] The issuer of the ETN had the right to repurchase the ETN's securities in the event of a substantial NAV decline. Because the "auto hold" was not disclosed to the ETN's sponsor and its investors, when real-time updates to the ETN's intraday indicative value were suspended due to the auto hold feature being activated, investors incorrectly assumed that the ETN would continue in existence despite the unprecedented volatility in the VIX markets and made additional purchases of the ETN while stale intraday index values were reported that resulted in greater losses. The SEC's rulemaking may impose additional oversight and due diligence responsibilities on advisers and funds that are designed to encourage disclosure of material features about the operation of an index and how its values are reported and errors in index calculations that may result or have resulted in investor losses.

This rulemaking is unlikely to involve investment adviser registration issues given the reference to index providers as "third party service providers" in the SEC Rulemaking Agenda. Former IM Director Dalia Blass previously suggested in a speech in March 2018 that an index provider for a "custom" index tailored to a single fund may not qualify for the "publisher's exception" under the Advisers Act and may need to register as an adviser.[16] To date, neither the SEC nor its Staff has provided additional public guidance about this position.

Possible Changes to the Current Regulatory Treatment of Fund Investments in Private Funds

Recent statements by the SEC, its Staff and others have indicated that regulatory changes may be on the horizon that would encourage investments in hedge funds or private equity funds (private funds) by funds.

[15] *In the Matter of S&P Dow Jones Indices LLC*, SEC Rel. No. 33-10943 (May 17, 2021), *available at:* https://www.sec.gov/litigation/admin/2021/33-10943.pdf.

[16] Keynote Address, ICI 2018 Mutual Funds and Investment Management Conference by Dalia Blass, Director, SEC Division of vestment Management (March 19, 2018), *available at:* https://www.sec.gov/news/speech/speech-blass-2018-03-19.

In July 2020, Dalia Blass, the former IM Director, announced that the Staff was re-examining a position that historically either limited investments in private funds by a closed-end fund when the fund was offered to retail investors, or required a fund that operated as a registered fund of funds to limit its offering to certain types of investors and impose a higher minimum investment requirement.[17] Under that Staff position, when a fund chooses to comply with the limitation on the fund's investment in private funds, the fund is required to disclose a limit of 15% of NAV on its investments in underlying private funds. For a registered fund of funds (which invests more than 15% of its NAV in private funds), the Staff position requires the fund to limit its offering to investors that qualify as "accredited investors" (AIs) as defined in Regulation D under the 1933 Act and impose a high minimum investment requirement.[18] In addition, no registered fund of funds has been permitted to list on an exchange.

The SEC issued a concept release regarding harmonization of exempt offering exemptions (Concept Release) in June 2019 that requested comments on increasing fund investments in private funds.[19] The focus of the Concept Release was on simplifying and harmonizing the exempt offering framework to encourage capital raising by issuers that typically access the private capital markets, with appropriate investor protections. As part of that analysis, the Concept Release explored whether the SEC should expand the ability of issuers to raise capital from pooled investment funds (including funds and private funds) and the ability of retail investors to access investments in growth stage issuers through pooled investment funds.[20] The Concept Release noted that certain funds are "better suited" than open-end funds for investments in less liquid or illiquid investments as they are not subject to the same liquidity restraints. Certain types of funds also have the potential to provide retail investors with some liquidity in the form of mandatory repurchase offers (in the case of interval funds) or discretionary tender offers (in the case of funds that rely on Rule 13e-4 under the 1934 Act).[21]

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[17] Speech at PLI Investment Management Institute by Dalia Blass, Director, SEC Division of Investment Management (July 28, 2020), *available at:* https://www.sec.gov/news/speech/blass-speech-pli-investment-management-institute.

[18] *See* Goldman Sachs Credit Income Fund and Goldman Sachs Real Estate Diversified Income Fund SEC Staff Comment Letter (filed Jan. 8, 2020) at p. 3 ("[Comment 12:] Please tell us how much the Credit Fund will invest in hedge funds and/or private equity funds that rely on section 3(c)(1) or 3(c)(7) of the 1940 Act. If the Credit Fund will invest more than 15% of its net assets in hedge funds and private equity funds that rely on sections 3(c)(1) or 3(c)(7), please note that registered closed-end funds that invest more than 15% of their net assets in such hedge funds or private equity funds should impose a minimum initial investment requirement of at least $25,000 and restrict sales to investors that, at a minimum, satisfy the accredited investor standard. Please confirm to us that the Funds will invest 15% or less or that they will impose a $25,000 initial investment minimum and will limit investments to accredited investors.").

[19] *Concept Release on Harmonization of Securities Offering Exemptions*, SEC Rel. No. IC-33512 (June 18, 2019), *available at:* https://www.sec.gov/rules/concept/2019/33-10649.pdf (Concept Release).

[20] *Id*. at 7 – 8.

[21] *Id*. at 174.

The Concept Release specifically requested comment on: (i) whether funds and business development companies regulated under the 1940 Act (BDCs) should be restricted in their investments in underlying private funds; (ii) what steps could be taken to enable mutual funds that are target-date funds to invest in underlying private funds; and (iii) whether funds and BDCs should be required to diversify their investments across a minimum number of private funds.[22] The Concept Release also sought comments on whether the rules that apply to interval funds and tender offer funds should be modified to change the periodic interval lengths or minimum repurchase amounts for interval funds, or change requirements applicable to tender offer funds.

At the AMAC meeting on March 23, 2021, the Private Investments Subcommittee (Subcommittee) considered potential options to encourage retail investor participation in private funds by easing limitations on private fund investments by certain types of funds, which would include listed closed-end funds, tender offer funds, interval funds, target date funds and registered funds of private funds (registered funds of funds). The AMAC was formed in October 2019 to provide the SEC with advice and recommendations from the perspective of representatives in the asset management industry, which include major fund sponsors. The Subcommittee considered the following public comments received on the Concept Release: (i) remove the 15% limit on closed-end funds investing in private funds; (ii) permit registered fund of funds to list on an exchange; (iii) increase the flexibility of interval funds and tender offer funds to invest in private funds; (iv) permit advisers of funds to be affiliated with underlying private fund sponsors; and (v) permit target date funds to have a greater percentage of their assets invested in private fund investments that decreases as the target date gets closer. Excluding private funds from existing liquidity requirements and permitting advisers of funds to have affiliations with private fund sponsors would likely require rule changes to be implemented, as the relevant restrictions that limit investments in private funds are imposed by rules under the 1940 Act or the 1940 Act itself.

At the AMAC meeting held on September 27, 2021, the Subcommittee issued its Final Report and Recommendations (Report)[23] on increasing retail investor access to private investments, which Report supports the use of the registered investment company framework to assist achievement of this objective. In this regard, the Report contains, among other things, recommendations consistent with certain comments on the Concept Release referenced above (*e.g.*, a change in the Staff's current position that a closed-end fund that holds more than 15% of its assets in private funds should only be offered to AIs; and increased flexibility for interval funds and tender offer funds to invest in private funds). The Report underscores that, under the current regulatory landscape, most retail investors are precluded from investing in the majority of private investments and strongly recommends that the SEC consider how to amend the regulatory framework to provide

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[22] *Id.* at 188.

[23] *See* SEC Asset Management Advisory Committee, Final Report and Recommendations for Private Investments (Sept. 27, 2021), *available at:* https://www.sec.gov/files/final-recommendations-and-report-private-investments-subcommittee-092721.pdf.

wider access to private investments by retail investors while maintaining appropriate safeguards for such investors.

S&K Observations/Insights: If the Staff position limiting fund investments in private funds is relaxed or rescinded, or the SEC proposes rule changes to implement suggestions received from commenters on the Concept Release, there are potential opportunities for asset managers to sponsor funds that use investments in underlying private funds more prominently in their strategies, and for registered fund of funds to offer their shares to additional types of investors that may not qualify as AIs.

Similarly, if these changes also apply to BDCs, BDCs could pursue more significant investments in underlying private funds. BDCs are subject to a regulatory framework under the 1940 Act that is substantially similar to that which applies to funds registered under the 1940 Act. The Staff position limiting investments to underlying private funds has been applied to BDCs, even though BDCs are already limited in the extent to which they can invest in private funds.

If the SEC were to implement AMAC's recommended changes to the regulatory landscape contained in the Report, the industry could see increased investments in closed-end funds, which currently represent a relatively small segment of the overall investment company market.

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If you have any questions regarding the items covered in this edition of Seward & Kissel Fund Industry Insights, please contact any of the attorneys listed below or your primary attorney in Seward & Kissel's Registered Funds Group.

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