The Increasing Investor Opportunities Act

Protect Closed-End Funds (CEFs) and Their Investors

Summary

The Increasing Investor Opportunities Act would remove a loophole that allows activist investors to take over closed-end funds (CEFs) and force them into liquidity events or radically change their investment strategy. It would also allow a CEF to invest its assets more freely in securities issued by private funds.

Background

CEFs are valuable financial products that provide investors—many of whom are American retirees—with steady, diversified streams of income. Yet despite their many benefits, CEFs face two tough challenges that are preventing retail investors from fully realizing the potential that these funds can offer:

- Sophisticated activists are taking over CEFs in pursuit of an agenda at odds with the interests of the funds' long-term retail investors; and
- An exchange-listed CEF may not freely invest in privately offered funds.

Why CEF Activism Is Dangerous

Activist investors are threatening CEFs and putting their long-term shareholders at risk. Under current law, these activist investors can acquire large positions—sometimes even a controlling interest—in a CEF, purchasing shares at a discount to the fund's net asset value. They then use their voting power to force the fund into a liquidity event, such as a tender offer, liquidation, or conversion to an open-end mutual fund, which makes money for the activist. Activist tactics undermine the core features that retail investors value in CEFs—such as exposure to a specific investment strategy or the ability to capture ongoing distribution income.

Increasing Access to Private Investments

In recent years, the SEC has sought to provide Main Street investors with greater access to private investments. CEFs are highly suitable vehicles for achieving the SEC's goal because they offer retail investors exposure to a diverse class of investments—including private investments—while maintaining the protections that publicly traded regulated funds provide.

Nevertheless, the SEC currently prohibits a CEF from investing more than 15 percent of its net assets in privately offered funds unless the CEF sells shares to accredited investors who make minimum initial investments of at least $25,000.

A Practical Solution

The bipartisan bill would restrict the amount of CEF shares that activist investors and their affiliates could acquire to no more than 10 percent, closing the loophole that activists exploit at the expense of CEFs' long-term shareholders. And it would prevent the SEC from unilaterally limiting how much CEFs can invest in privately offered funds.

The Bottom Line

ICI urges Congress to pass this bipartisan legislation to protect and increase opportunities for US retail investors through CEFs.

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