



## Activism Isn't Waning, But Rules Governing It Are Changing

Friday, December 10, 2021

Chuck Jaffe, in this episode of The NAVigator podcast interviewed Thomas DeCapo, partner at Skadden, Arps – one of the largest law firms representing interests in the closed-end fund industry. Read the Q & A below as Thomas discusses developments and changes to the activist environment, noting that one thing he believes will not change is the high level of activity due to the many funds facing activists with stakes of 10 percent or more. DeCapo also discusses



industry rumors that regulators are considering changing control-share statutes that have a major impact on how closed-end funds are governed.

Thomas DeCapo

The podcast can be found on AICA's website by clicking here: <https://aicalliance.org/alliance-content/pod-cast/>

**CHUCK JAFFE:** Attorney Thomas DeCapo is here and he's talking about the current activist environment in closed-end funds, and this is The NAVigator. Welcome to The NAVigator, where we talk about all-weather active investing and plotting a course to financial success with the help of closed-end funds. The NAVigator is brought to you by the Active Investment Company Alliance, a unique industry organization that represents all facets of the closed-end fund industry. From users and investors to fund sponsors, creators, and well yes, lawyers, because that's where we're going today. We're discussing some of the behind the scenes stuff

that does affect fund activism with Tom DeCapo, partner at Skadden, Arps, Slate, Meagher & Flom, and they're online at [Skadden.com](http://Skadden.com). To learn more about closed-end fund investing generally go to [AICAlliance.org](http://AICAlliance.org), the website for the Active Investment Company Alliance. Tom DeCapo, thanks for coming back to The NAVigator.

**THOMAS DeCAPO:** Well Chuck, thanks for having me, it's always nice to speak with you.

**CHUCK JAFFE:** Tom, there have been some interesting developments and then there's some rumors about things that might be happening that we'll get into later, but let's just take a quick look. Because I know we have talked to activists before who have been saying the activist environment is changing. From your perspective, because you're in it from the legal side, what's going on now and what does it mean for the future here?

**THOMAS DeCAPO:** Sure, thank you. We're seeing a lot of activity. The activists are keeping the fund groups and ourselves busy so the situation continues apace. There are many funds out there that have activists with stakes that are above the 10%, approaching the 20% or more level. And so I would expect over the course of the upcoming annual meeting and proxy season, and probably the following one, for things to continue to be busy. And yes, in addition to being busy they also are changing. One example, this one's a little bit old but I think it was last year we had a fund, rather than the usual model of providing some type of liquidity event, instead the activists obtained control of the board and the activist advisor was appointed as the advisor for the fund. The fund now continues on managed by the activist. More recently we have a fund that offered, this fund is not our client. And actually while I say that I should say the views I express here are mine, they're not Skadden, Arps. I have clients involved in some of these types of matters and you can expect that the views that I express are not going to be at odds with what I would expect my clients views to be, so that's just common sense but I should mention in. In any event, this more recent situation a fund offered a tender offer for 70% of its outstanding shares at a price of 99% of NAV. Historically that would be viewed as a very attractive resolution to the activists. The activist involved there who owned over 20% of the fund announced that they were not going to participate. That in their mind because many funds of this type were actually trading at a premium to NAV, that small discount was insufficient and they were not going to participate in the tender. That's a pretty new development and maybe gives us a signal of where things are headed in the future.

**CHUCK JAFFE:** Yeah, that's particularly interesting. But there have been some other surprises in how some of these situations have turned out recently too, haven't here?

**THOMAS DeCAPO:** Well, there have been. You can never be sure what's going to happen until you've had the vote, and there have been some situations recently where some activists who didn't own shares prior to the record date of the meeting coming up getting involved in the meeting and soliciting no votes even though they hadn't previous had a stake in the fund. So to some degree it's unscripted and real time, and you don't know what happens until it happens.

**CHUCK JAFFE:** Let's talk about a different kind of fight. There is a lot of talk around what has been happening with the control-share statutes, state control-share statutes. We've talked about them in the past when you were on The NAVigator, and this is a really important issue that without getting political some of it was fostered by the last administration. So there's at least talk that maybe the current administration or the current SEC staff feels a little bit differently. Have you heard anything about the SEC wanting to change what's going on?

**THOMAS DeCAPO:** It's a very interesting topic. It has been in play literally for decades. So one would think, or at least I would think, that by now we'd have a pretty solidified policy position and legal position on it. But maybe not. I have not been involved in any direct discussions with any staff members that lead me to believe that they are thinking about changing their views on this topic. But I have, as you just mentioned, heard some people in the industry secondhand who have heard rumors that that might be the case. I certainly hope it isn't the case. I believe it would be a big step in the wrong direction indeed for my point of view, and again this is me speaking as one individual out here, but in my point of view it should be going the other way. When I take a step back, and I've been in the fund industry working as a lawyer with funds now for over 30 years, when I take a step back and I think about it, what is a fund? A fund is an individual investment account for all practical purposes, that's done on a mass basis so that retail investors can access professional management in strategies that they need help in. And so on a cost-effective basis where they wouldn't be able to individually go out for few thousand dollars and hire a professional manager for themselves. That's what a fund is. Open-end funds, you get in and out of them every day and the cost of that is they're not allowed to invest very heavily in illiquid securities or pursue investment strategies that make it difficult to provide daily redemptions. Closed-end funds

are just like open-end funds, there's a practical matter, they're there to again provide this professional investment advice to retail investors. But because the closed-end fund doesn't have to let investors out every day, they get to pursue from a regulatory perspective, other strategies that are less liquid and over the long term should have higher returns and to use leverage which again over the long term should produce higher returns. And as an accommodation to investors because they can't get out of a closed-end fund through the fund every day, they get liquidity by listing those shares on an exchange. Well, to my mind I don't see why that fact should cause funds to be treated like operating companies subject to all of the voting and corporate governance requirements of an operating company. As between an operating company and an exchange traded fund, a closed-end fund looks a lot more like an exchange traded fund than it does an operating company. Exchange traded funds are exempted from those requirements of having annual meetings. And so I would hate to see the position on control share statutes start to drift back the other direction where not only are funds treated like operating companies for purposes of having annual meetings, and votes on directors, and potential fights with activists, but on top of that they're denied the ability to defend themselves like operating companies can under state law. I think that would just be a terrible result.

**CHUCK JAFFE:** I don't think that's good for anybody in the fight. If you change the rules and you make it the requirements are fewer meetings and less ability to talk back and all the rest, I think both sides lose. Don't they?

**THOMAS DeCAPO:** I'm not so sure. The Investment Company Act is a specific body of law designed to regulate investment companies, and it sets out voting requirements for those important subject matters about funds. Including most importantly the shareholder's right to remove the investment advisor. And I would argue that the Investment Company Act sets out all the corporate governance requirements that you need. Subjecting a closed-end fund to the corporate governance requirements of the New York Stock Exchange simply because shareholders get to get liquidity in the open market is a gigantic distraction that runs the risk of taking away from retail investors their ability to get access to asset managers that they need. And so while it would be a big change, I don't know that it would be a bad change. As between going back to where we were, which is closed-end funds with two hands tied behind their back as they're forced to function like operating companies but can't avail themselves

of the state law rights that operating companies can, or treating them more like ETFs. I would say that treating them more like ETFs makes a lot more sense.

**CHUCK JAFFE:** Tom, really, really interesting. Thanks so much for joining me to talk about it.

**THOMAS DeCAPO:** Happy to do it anytime, Chuck. Thank you very much.

**CHUCK JAFFE:** The NAVigator is a joint production of the Active Investment Company Alliance and Money Life with Chuck Jaffe. Yep, that's me and you can check out my hour long weekday show on your favorite podcast app or at MoneyLifeShow.com. To learn more about interval funds, closed-end funds, and business-development companies go to AICAlliance.org, the website for the Active Investment Company Alliance. They're on Facebook and LinkedIn @AICAlliance. Thanks to my guest, Thomas DeCapo, partner at Skadden, Arps, Slate, Meagher & Flom and Affiliates. They're online at Skadden.com and on Twitter @SkaddenArps. The NAVigator podcast is new every Friday, ensure you don't miss a thing by subscribing via your favorite podcast app. And until we do this again next week, happy investing everybody.

*Recorded on December 9th, 2021*

To request a particular topic for The NAVigator podcast please send an email to: [TheNAVigator@AICalliance.org](mailto:TheNAVigator@AICalliance.org)

Click the link below to go to the home page of Active Investment Company Alliance to learn more: <https://AICalliance.org/>

**Disclosure:** *Listed closed-end funds and business development companies trade on exchanges at prices that may be above or below their NAVs. There is no guarantee that an investor can sell shares at a price greater than or equal to the purchase price, or that a CEF's discount will narrow or be eliminated. Nonlisted closed-end funds and business development companies do not offer investors daily liquidity: often on a small percentage of share on a quarterly or semi-annual basis. CEFs often use leverage, which can increases a fund's risk or volatility. The actual amount of distributions may vary with fund performance and other conditions. Past performance is no guarantee for future results.*