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BY EMAIL

Vanessa A. Countryman, Secretary
Securities and Exchange Commission
100 F Street, NE
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RE: File No. SR-NYSE-2024-35

Proposed Rule Change Amending Section 302.00 of the NYSE Listed Company Manual to Exempt Closed-End Funds Registered Under the Investment Company Act of 1940 from the Requirement to Hold Annual Shareholder Meetings[1]

To the Securities & Exchange Commission ("SEC"):

Let's call this Proposal what it is: a naked and not particularly creative attempt by the industry, and its representatives at the Investment Company Institute ("ICI"), to entrench the worst quartile of fund advisers after their prior illegal defensive mechanisms were struck down by the courts.[2] The thinking is simple: if we can't rig the vote, then let's not have a vote. This warped

[1] This comment is made in connection with the July 3, 2024 proposed rule change as to Section 302.00 of the NYSE Listed Company Manual, Release No. 34-100460 (the "Proposal"). The views expressed herein are my own and do not necessarily reflect the views of my law firm or its partners and clients.

[2] *See Saba Capital Master Fund, Ltd. v. BlackRock Municipal Income Fund, Inc.*, 2024 WL 43344 (S.D.N.Y. Jan. 4, 2024), *aff'd* 2024 WL 3174971 (2d Cir. June 26, 2024) (use of control share defense violates Section 18(i) of the Investment Company Act of 1940); *Saba Cap. CEF Opportunities 1, Ltd. v. Nuveen Floating Rate Income Fund*, 2022 WL 493554 (S.D.N.Y. Feb. 17, 2022), *aff'd* 88 F.4th 103 (2d Cir. Nov. 30, 2023) (same). The courts are virtually certain to rule the same as to the use of a "poison pill" defense by investment companies. *See Saba Capital Master Fund, Ltd., et al. v. ASA Gold and Precious Metals, Ltd.*, No. 24-cv-690 (JGLC). ICI's prior legal "analysis" provided to the Commission on these defensive mechanisms was so biased and wrong that its views in the future should be afforded no weight. *See* December 16, 2020 ICI Letter at 5

form of "corporate governance," if it can be called that, has no place in the public markets, and the rationales fabricated by the Proposal are fiction.

A. The 1940 Act Protections Cited By The Proposal, As Currently Applied, Do Not Substitute For The NYSE's Annual Meeting Requirement

1. The "Right" To Elect Directors Under Section 16(a). The Proposal states that "there are significant differences between CEFs and listed operating companies that justify exempting CEFs from the Exchange's annual meeting requirement," including primarily that "Section 16(a) of the 1940 Act specifies the right of CEF shareholders to elect directors." In practice, however, the industry, with the SEC's help, has neutered that provision by taking the legally erroneous position that a fund's board of directors can be chosen and elected solely by the *fund's investment manager* prior to issuing public shares, after which no further election by the public stockholders is required. As described by the ICI, the adviser is typically the "initial shareholder through the seed money" and "recruits unaffiliated persons to serve as independent directors," which the adviser unilaterally elects in its capacity as sole shareholder.[3] Indeed, in response to a no-action request from the ICI, the SEC stated that it would "no longer require an undertaking to conduct a meeting to elect directors" by its "public shareholders, not just its initial shareholders," under the rationale that "public shareholders have voted with their dollars."[4] Whether that logic holds as to open-end funds (with full liquidity at NAV) is tenuous, but it certainly does not work with closed-end funds where the assets are captive and shareholders are required, in many instances, to sell at an enormous discount just to get out.[5] In any event, the stockholder "right" to elect directors under the 1940 Act, as it is currently being effectuated, does not substitute for the NYSE's annual meeting requirement.

2. The Independent Director Requirement. The Proposal also cites the 1940 Act requirement that "a majority of directors who are not 1940 Act Interested Persons approve significant actions, such as approval of the investment advisory agreement between a CEF and its

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("[F]und defenses involving voting rights provisions (*e.g.*, implementing poison pills and opting into control share statutes) . . . do not violate Section 18(i)").

[3] Investment Company Institute, How U.S.-Registered Investment Companies Operate at 7.

[4] SEC No-Action Letter, 1992 WL 400454 (Nov. 6, 1992).

[5] Setting aside the SEC's logic, its position was never consistent with the plain language of Section 16(a), which requires that directors be "elected to that office by the holders of the outstanding voting securities." Nevertheless, the position has empowered legacy directors to simply ignore stockholders and the 1940 Act, and cling to their positions even when stockholders refuse to elect them. *See, e.g., Saba Capital Master Fund, LTD. v. Blackrock ESG Capital Allocation Trust, et al.*, No. 1:24-cv-01702-MMG (S.D.N.Y.).

investment advisor." This too, in practice, is an empty protection that does not support eliminating the NYSE's annual meeting requirement. The so-called "non-interested" fund directors are at the *very core of the problem* in closed-end funds, and the 1940 Act's reliance on fund directors to do anything other than exactly what the adviser suggests is its biggest failure.[6] Aside from a few strong-willed personalities (eventually run out on a rail), the average fund director has been conditioned beyond salvation to "review information," "ask questions," "consider all factors" (but never forget that "no single factor is determinative") and rubberstamp everything on the agenda as fast as the lawyers can copy and paste.[7] The "fiduciary" duties owed by fund directors have become an open and notorious joke among the cadre of lawyers and service providers that inhabit the investment company ecosystem.[8]

We have observed "independent" directors choose the adviser's financial interests over those of stockholders time and time again. For example, in litigation involving adviser misconduct, independent directors routinely align with the adviser in the defense of the case, regardless of the merits, even though a recovery would directly benefit stockholders. In the case of the Fiduciary/Claymore Energy Infrastructure Fund, a closed-end fund, the portfolio was overleveraged by the adviser and incurred losses of more than 80% after the adviser dumped most of the portfolio to meet margin calls during market turbulence.[9] What's worse, the adviser was not

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[6] *See* Alan R. Palmiter, *The Mutual Fund Board: A Failed Experiment in Regulatory Outsourcing*, 1 BROOK. J. CORP. FIN. & COM. L. 165, 171 (2006) ("[M]ost fund boards are composed of industry-friendly, highly paid, long-serving directors. The lack of independence of mutual fund directors, even those who carry the label 'not interested,' has long been an open secret."); Joseph A. Warburton, *Should Mutual Funds Be Corporations? A Legal & Econometric Analysis*, 33 J. Corp. L. 745, 753 (2008) ("The system of mutual fund directors has faced mounting criticism of the years, leading to claims that they are not 'watchdogs' but rather 'sleeping dogs.' As tangible evidence, critics typically point to directors' failure to keep management fees low, to terminate management contracts with poorly performing investment advisers, and to effectively challenge practices of investment advisors.").

[7] "Very occasionally a board will revolt. But for the most part, a monkey will type out a Shakespeare play before an 'independent' mutual-fund director will suggest that his fund look at other managers, even if the incumbent manager has persistently delivered substandard performance." Warren Buffet, 2002 Letter to Berkshire Hathaway, Inc. Shareholders. *See also* CNBC, 'Mediocre' Gross Overpaid At $200 Million: Trustee (independent trustee criticizing adviser compensation); Los Angeles Times, Longtime Trustee Of PIMCO Mutual Funds Appears To Have Lost His Job (same independent trustee removed from board).

[8] Stewart L. Brown, PhD., CFA, *Mutual Fund Advisory Fees: An Objective Fiduciary Standard*, 21 U. PA. J. BUS. L. 477 (2019) (quoting Jack Bogle as testifying that "fund directors are, or at least to a very major extent, sort of a bad joke").

[9] *JB and Margaret Blaugrund Foundation v. Guggenheim Funds Investment Advisers, LLC et al.*, C.A. No. 2021-1094-NAC (Del. Ch.).

aware of enormous tax implications caused by the fire sale, and concealed for three quarters that the fund would have to write down its NAV by an additional 40%. In the aftermath, the fund's independent directors purportedly found nothing wrong with the adviser's conduct, did nothing to mitigate the losses or hold the adviser accountable, renewed the adviser's contract on the same terms, and actively opposed claims by stockholders. Then, in anticipation of litigation, the board rubberstamped a merger with another closed-end fund, at the adviser's request, which eliminated the fund and its litigation claims for no compensation (*i.e.*, $0). The directors did not even consider negotiating for consideration for stockholders in the merger. Stockholders were left to pursue contentious litigation against the independent directors and adviser for years before making an $18.8 million recovery.[10] Directors have consistently taken the same tack in other cases involving misconduct until held accountable by stockholders through litigation.[11]

The Proposal's invocation of director oversight is particularly ironic given that the non-interested directors fight the hardest (and dirtiest) to oppose stockholder initiatives during the currently required annual meetings. For example, consider the Templeton Global Income Fund managed by Franklin Advisers, Inc. When it appeared that stockholders would elect a slate of four new directors at the annual meeting, the independent trustees permitted Charles Johnson, the former CEO of the Franklin, and the *fund itself* to sue the nominating stockholder on baseless allegations about a purportedly "secret" agreement with another stockholder. The court promptly rejected the fund's motion for an injunction because its assertions were "speculative, not imminent, and not concrete."[12] The directors filed an "emergency" appeal, and shortly thereafter gave up, but not before causing significant legal expenses for the nominating stockholder.

Similarly, in a case involving a group of poorly performing bond funds managed by UBS, the stockholder's nominees were expected to easily defeat the incumbents at the annual meeting. In response, the independent directors caused *nine funds* to sue the stockholder and various other persons under baseless securities fraud claims. The case was dismissed in its entirety and judgment entered in favor of the stockholder.[13] However, the incumbents still refused to allow the new, validly elected directors to join the board until the court issued a second ruling instructing them to

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[10] May 10, 2024 Notice of Proposed Settlement.

[11] Shareholders similarly made recoveries in at least the following cases on their own without the support of the independent directors: Morgan Keegan Funds, The Reserve Primary Fund, Van Kampen Prime Rate Income Trust, State Street Yield Plus Fund, Eaton Vance Floating-Rate Funds, First Trust High Income Funds, Evergreen Ultra Short Opportunities Fund, Fidelity Ultra-Short Bond Fund, Heartland Municipal Bond Funds and Third Avenue Focused Credit Fund.

[12] *Johnson v. Saba Cap. Mgmt., L.P.*, 2023 WL 1345717, at *4 (S.D.N.Y. Jan. 31, 2023).

[13] *Tax-Free Fixed Income Fund for Puerto Rico Residents, Inc. v. Ocean Cap. LLC*, 2023 WL 5835786 (D.P.R. Aug. 10, 2023), adopted, 2023 WL 5830381 (D.P.R. Sept. 8, 2023).

do so.[14] These are only a few examples demonstrating that fund directors provide no subsitute for the direct expression of stockholder viewpoints through an annual meeting.[15]

3. Required Stockholder Approval of Certain Matters. Finally, the Proposal cites certain 1940 Act provisions requiring stockholders to approve (i) new or materially amended investment management agreement; (ii) a change from closed-end to open-end status or vice versa; (iii) a change from diversified company to non-diversified company; (iv) a change in, or deviation from, certain investment policies; and (v) a decision to stop being an investment company. As above, these "rights" do nothing to substitute for the NYSE's annual meeting requirement.

As to point (i), the investment management agreement is approved by the initial board and investment manager itself, not public stockholders, and decades of actual practice have shown that a management agreement will never change unless and until the adviser determines that doing so would be profitable to itself or its parent. For example, directors will rubberstamp a renewed advisory agreement for years, but, on a dime, will readily approve a new management contract with a third party in connection with an acquisition of the current investment adviser, through which the adviser or its parent will derive a profit.[16] Directors are so subservient that they will even approve the new contract, without negotiation, when their own positions are being eliminated through a complex and board reorganization.

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[14] *Tax-Free Fixed Income Fund for Puerto Rico Residents, Inc. v. Ocean Cap. LLC*, 2024 WL 3384992 (D.P.R. July 11, 2024).

[15] *See also, e.g., JID 2013 Trust Holdings LLLP v. Tortoise Energy Independent Fund, Inc.*, No. 1:24-cv-02004 (D. Md. 2024) (pending litigation where independent directors reduced the board size immediately after receiving stockholder nominations to avoid losing a seat); *Goldstein v. Lincoln Nat'l Convertible Sec. Fund, Inc.*, 140 F. Supp. 2d 424 (E.D. Pa. 2001) (holding that independent directors breached their fiduciary duties by staggering the board and implementing an improper advanced notice provision after a stockholder made director nominations).

[16] Warren Buffett observed this phenomenon in his 2003 letter to shareholders: "Year after year, at literally thousands of funds, directors had routinely rehired the incumbent management company, however pathetic its performance had been. Just as routinely, the directors had mindlessly approved fees that in many cases far exceeded those that could have been negotiated. Then, when a management company was sold—invariably at a huge price relative to tangible assets—the directors experienced a 'counter-revelation' and immediately signed on with the new manager and accepted its fee schedule. In effect, the directors decided that whoever would pay the most for the old management company was the party that should manage the shareholders' money in the future." *See also* Palmiter, *supra* n. 6, at 191 (Contractual renegotiations are "rare event[s]" that happen in only 10% of funds."); Warburton, *supra* n. 6, at 756 (citing only three historical instances in which "independent directors refused to approve management contracts and the issue subsequently fell to shareholders").

As to points (ii) through (v), these are fundamental changes that, again, decades of practice demonstrate that the adviser will never propose unless doing so would be profitable to itself or its parent, and thus these "rights" rarely result in a substantive benefits for stockholders.[17] For example, as part of a "strategic repositioning" in 2021, the Affiliated Managers Group (AMG) opted to cannibalize assets from unaffiliated subadvisers and convert the funds into new strategies that could be managed internally by its own affiliates, resulting in a net increase in fees to AMG. Stockholders were asked to approve the conversions under various rationales concocted by the board at the time.

An annual meeting is an exceedingly more valuable and practical right than those discussed above because it affords some measure of control over the long-term direction of the fund—a right that stockholders have held and come to expect for a century.

B. The Three (Of Twenty Five) Comments Supporting The Proposal Are Telling

Of the twenty five comments submitted at the time of this submission, *only three* support the Proposal, all of which appear to be industry representatives.

In a July 17, 2024 submission, Kevin Coroneos claims to be a "closed-end fund (CEF) investor" without mentioning that he's also the ICI's Director of Digital Advocacy Strategy. In his comment, he parrots the ICI's recent publication suggesting that activism is the cause of a decline in new closed-end funds, and not the perpetual trading discounts, high fees, and out-of-touch legacy managers that lack the ability to outperform index funds.[18] Amusingly, Mr. Coroneos describes corporate democracy—and the foundational right of stockholders to elect managers—as a mere "loophole," and suggests no such rights are required because "[t]here will still be elections for an initial board" *by the investment manager* when it seeds the fund. Mary Wilber's July 18, 2024 comment, which also opposes the Proposal, is materially identical and suggests an affiliation.

In a July 17, 2024 comment, Kim Anderson, a senior vice president at Voya Investments, argues that "[a]s an investor in closed-end funds, [she has] experienced the negative results of activist investors," but fails to mention that *she works for the investment manager* that fought a proxy contest with the activist she criticizes, and lost.[19] Ms. Anderson claims that the activist "took

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[17] Reuters, Fired Fund Manager Friess Battles AMG Over Brandywine Portfolios (April 22, 2021).

[18] *Compare* July 17, 2024 Coroneos Comment ("Activist activity is making the CEF market unsustainable. In fact, not a single new CEF was launched last year.") *with* ICI, Closed-End Fund Activism Surges, Shows Need for Congressional Action ("[I]ncreased shareholder activism has impacted the market so much that no new traditional CEFs opened for the first time in more than a decade").

[19] It is telling that Ms. Anderson submitted a second comment on July 23, 2024 stating that she "did not understand that my name, title and employer would be made public," confirming that it was her intention to conceal her affiliation with Voya.

over" the Voya Prime Rate Trust (former ticker: PPR) for its "own gain." But Voya had been operating the fund for its "own gain" for years, and the activist, which owned only 25% of outstanding shares, petitioned the other 75% of stockholders for change. The new directors were supported broadly by unaffiliated stockholders,[20] and Voya knew it could not win a stockholder vote, so the so-called "independent" incumbents *attempted to rig the vote* by amending the fund's bylaws to implement an effectively impossible election threshold for new directors—60% of all outstanding shares when the standard since inception was a plurality of votes. A trial court struck down the new voting standard because it was "impossible" and obviously intended to prevent "new trustees from being elected" and "entrench [] the existing trustees."[21] After the new directors were validly elected by stockholders, Ms. Anderson notes that the new board "fired" Voya (*i.e.*, her firm), "appointed Saba as the adviser," and "changed the strategy," but she fails to mention that stockholders *approved these changes by a margin of 95%*.[22]

As reflected above, the industry's own commentary demonstrates that the Proposal is a job-protection measure for underperforming advisers that are tired of hearing from stockholders.

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The SEC must draw a line somewhere north of rendering every closed end fund a perpetual treasure trove for incumbent advisers. If the SEC is unwilling to rethink its erroneous interpretations of Sections 18(i) and 16(a), then it certainly should not eliminate the semblance of corporate democracy currently created by the NYSE listing rules.

Sincerely,

Aaron T. Morris

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[20] It is undisputed that the vast majority of unaffiliated stockholders voted for the new nominees and rejected Voya's incumbents. Ms. Anderson feigns outrage that the nominees were "hand-picked by Saba" when, at the same time, the incumbents were "hand-picked" by Voya. It is truly "laughable," to use her term, to think that any incumbent was ever independent of Voya.

[21] *See Saba Capital CEF Opportunities 1 Ltd v. Voya Prime Rate Trust*, 2020 WL 5087054, at *6 (Ariz. Super. June 26, 2020).

[22] Business Wire, Voya Prime Rate Trust Announces Results of Special Meeting of Shareholders (May 25, 2021). It is also worth noting that advisers routinely take these actions for themselves, but Ms. Anderson appears to object only when stockholders take a turn. *See* n. 14 & 15, *supra*.