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Skadden

Investment Management Alert

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Activists Take Another $290 Million Bite Out of Vulnerable Closed-End Fund Asset Class

On June 14, 2019, Saba Capital Management, L.P. (Saba) entered into three standstill agreements with Invesco Advisers, Inc. (Invesco) and three Invesco-managed registered closed-end funds. The agreements arose from proxy contests that Saba initiated in an effort to coerce the funds into liquidating, converting into open-end funds or shrinking in size through at-or-near-net-asset-value (NAV) "liquidity events." These coerced events will allow Saba and its hedge fund investors to make a short-term profit based on the fund's market price discount from NAV, at the expense of the fund's long-term retail investors. In connection with the proxy contests, Saba had proposed slates of its own trustee nominees to fill seats on each fund's board and submitted shareholder proposals to seek shareholder votes to declassify the funds' boards of trustees.

The standstill agreements were announced on the heels of Saba escalating its activist tactics in another, concurrent proxy contest with three BlackRock closed-end funds by filing state court lawsuits against these funds, the trustees/directors of the funds and their investment adviser, and seeking class action certification. As noted in our June 7, 2019, client alert "Class Action Proxy Litigation Highlights Need for Corporate Defense Strategies in Closed-End Funds," Saba similarly seeks in these BlackRock proxy contests to elect its own slates of trustees/directors to the funds' boards and to declassify two of the funds' boards.

Saba's attacks on the closed-end fund community appear to be paying off well for the company and its hedge funds: As part of the Invesco standstill agreements, the funds' boards agreed to cause the funds to commence tender offers to repurchase either 15% (with respect to two of the funds) or 20% (with respect to one of the funds) of their outstanding common shares, at a price equal to 98.5% of net asset value. If fully subscribed, which is virtually assured when a high proportion of shares are held by short-term profit-seeking activists, the tender offers will eliminate another $290 million in exchange-traded closed-end fund assets. In return, Saba agreed to withdraw its proposed nominees and its proposals to seek shareholder votes to declassify the boards. The agreement confirms that such proxy contests and related lawsuits are not about "good governance" or any other salutary purpose but rather, about coercing closed-end funds that cannot adequately protect themselves into delivering a short-term profit for Saba, other activists and their hedge fund investors, at the expense of the long-term retail investing public.

As we recently noted, closed-end funds' ability to fend off these abusive tactics has been hamstrung by historical Securities and Exchange Commission (SEC) staff positions1 regarding the use of common corporate defense measures that may be available in the world of ordinary operating companies, such as shareholder rights plans and state law control share statutes. These measures are not intended as management entrenchment devices, but rather to encourage would-be acquirers of a company's shares that are looking to obtain control of a company to do so by negotiating with the company's management — which is responsible for acting in the best interests of all shareholders — rather than by purchasing shares on the open market, acting only in their own interests and to the detriment of the company's long-term shareholders. We believe that the current SEC staff is more understanding of the benefits closed-end fund provide to the investing public, and may be more receptive to protecting closed-end funds, than has been the case for over a decade.

In light of the increasingly aggressive tactics activist closed-end fund investors are using in order to coerce funds into providing at or near net asset value short-term profit "liquidity events" to the detriment of long-term retail shareholders, closed-end fund boards should reevaluate shareholder rights plans, state law control share statutes and other corporate defense strategies. They should do so in order to preserve retail investors' access to closed-end funds and the unique exposure they provide to asset classes and strategies that retail investors may not be able obtain elsewhere.

We would be happy to discuss our views as to the legal basis, process and timing for considering and implementing defensive strategies, including shareholder rights plans and state law control share statutes in closed-end funds.

[1] *See* Boulder Total Return Fund, Inc., SEC Staff No-Action Letter, 2010 WL 4630835 (Nov. 15, 2010); Andrew J. Donohue, Director, SEC Division of Investment Management, Keynote Address at the Independent Directors Council Investment Company Directors Conference (Nov. 12, 2009).