

THE REVIEW OF  
**SECURITIES & COMMODITIES  
REGULATION**

AN ANALYSIS OF CURRENT LAWS AND REGULATIONS  
AFFECTING THE SECURITIES AND FUTURES INDUSTRIES

Vol. 57 No. 3 February 7, 2024

## CLOSED-END FUND ACTIVISM: HOW TO LEVEL THE PLAYING FIELD

*The dramatic increase in the scope, tone, tactics, goals and impacts of closed-end fund shareholder activism is strangling an important investment product for middle-class retail investors, including retirees. In this article, the author discusses areas where either Congress or the SEC can act to protect retail closed-end fund investors, including by passing H.R. 2627, The Increasing Investor Opportunities Act, or through public guidance and rulemaking.*

By Kenneth E. Burdon \*

The Investment Company Act of 1940 regulates investment companies offered to and purchased by public retail investors. The Act is the result of a comprehensive effort following the 1929 stock market crash to eliminate abuses in the securities industry and is the product of a congressionally ordered study conducted by the Securities and Exchange Commission. The historical context of abuses out of which the Investment Company Act grew was so important that Congress inserted, as Section 1 of the Act, an enumeration of these abuses and a statement that the “policy and purposes” of the Investment Company Act are “to mitigate and, so far as is feasible, to eliminate” the abuses enumerated in Section 1, and that the provisions of the Investment Company Act “shall be interpreted” in accordance with such policy and purposes.<sup>1</sup>

Key abuses enumerated in Section 1 of the Act include:

(b)(2) when investment companies are organized, operated, managed, or their

portfolio securities are selected, in the interest of . . . affiliated persons thereof, . . . or in the interest of other investment companies . . . , rather than in the interest of all classes of such companies’ security holders; . . . [or] (4) when the control of investment companies is unduly concentrated through pyramiding or inequitable methods of control or is inequitably distributed, or when investment companies are managed by irresponsible persons.

Of note, an “affiliated person” of an investment company is defined in section 2(a)(3)(A) of the Act to include individuals or entities who directly or indirectly own, control, or hold with power to vote, 5% or more of the outstanding voting securities of the investment company. Therefore, a key policy objective of the Act is to protect retail shareholders of investment companies from overreaching, or undue influence, by concentrated shareholders who may seek to enrich themselves at the expense of retail shareholders — and these concentrated shareholders may exercise such undue influence with as little as a 5% holding.

<sup>1</sup> Investment Company Act § 1(b).

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