

Chapman Client Alert

March 29, 2019

Current Issues Relevant to Our Clients

SEC Proposes New Rules for Closed-End Fund and Business Development Company Security Offerings

On March 20, 2019, the U.S. Securities and Exchange Commission (the “SEC”) voted to propose amendments to existing rules and forms under the Securities Act of 1933 (the “Securities Act”), the Securities Exchange Act of 1934 (the “Exchange Act”) and the Investment Company Act of 1940 (the “Investment Company Act”) that, if adopted, would modify the registration, communication, offering and reporting processes applicable to registered closed-end investment companies (“closed-end funds”) and business development companies (“BDCs”) regulated under the Investment Company Act. The proposed amendments would, among other things:

- Streamline the registration process for closed-end funds and BDCs to mirror that available for operating companies, including by allowing short-form shelf registration statements and forward-incorporation of Exchange Act reports;
- Provide eligible closed-end funds and BDCs with the ability to qualify as well-known seasoned issuers (“WKSIs”), which would provide such funds with the ability to file automatic shelf registration statements;
- Harmonize the public communication rules of closed-end funds and BDCs with those of operating companies, including the ability to use “free writing prospectuses” and other pre-effective communications; and
- Expand existing closed-end fund and BDC reporting requirements with new periodic and current reporting requirements.

The amendments are being proposed by the SEC pursuant to the mandates included in both the Small Business Credit Availability Act and the Economic Growth, Regulatory Relief and Consumer Protection Act. The full text of the proposal is available [here](#). The following is a summary of principal changes to existing rules and forms.

Amendments to Closed-End Fund Registration and Offering Rules

Under existing Securities Act rules, certain issuers that meet the eligibility requirements of Form S-3 are able to register securities on a “shelf” registration statement and conduct offerings of such securities “off the shelf” under Securities Act Rule 415(a)(1)(x) at a time of an issuer’s choosing. Currently, closed-end funds and BDCs may register and offer their securities pursuant to these procedures if they meet the applicable eligibility criteria to use Form S-3. However, such funds are disadvantaged when conducting offerings pursuant to a shelf registration statement compared to operating companies. Eligible operating companies are permitted to use a short-form registration statement on Form S-3 and may rely on Securities Act Rule 430B to omit certain information (including the plan of distribution and information regarding

selling security holders) from the “base” prospectus when the registration statement becomes effective and later provide certain information in subsequent Exchange Act reports incorporated by reference, a prospectus supplement or a post-effective amendment. In contrast, closed-end funds and BDCs are not permitted to use a short-form registration statement or forward-incorporate information from subsequently filed Exchange Act reports. Accordingly, when a closed-end fund or BDC sells securities, including as part of an off-the-shelf offering, its registration statement must include all required information, including current financial information, at or around the time of effectiveness. Further, such a fund must provide any updates to its registration statement through a post-effective amendment, which can incur expenses and cause delays in the offering process. Absent the fund obtaining no-action relief providing for automatic effectiveness for certain post-effective amendments, such amendments would also be subject to the SEC staff’s review and comment process.

The proposed amendments would permit closed-end funds and BDCs to file a short-form registration statement on Form N-2 that would function like the short-form registration statement filed on Form S-3 by operating companies and allow such funds to rely on Rule 430B to omit certain information from the registration statement at the time it becomes effective. The short-form registration statement would incorporate certain past and future Exchange Act reports by reference, thus allowing a fund to avoid the need to make a post-effective amendment in many cases (e.g., updating financial information). A closed-end fund or BDC would be generally eligible to file on a short-form registration statement if (1) it has timely filed all reports and other materials required under the Exchange Act during the prior year, (2) the fund's "public float" is \$75 million or more, and (3) the fund had been registered under the Investment Company Act for at least twelve calendar months immediately preceding the filing of the registration statement and has timely filed all Investment Company Act reports during that time.

The proposed amendments would also permit closed-end funds and BDCs that would qualify as WKSIs under the proposed amendments to file an automatic shelf registration statement that becomes effective immediately upon filing, providing a greater degree of flexibility with respect to timing of offerings. Eligible closed-end funds and BDCs would also be able to take advantage of the "pay-as-you-go" registration fee rules, which grant WKSIs the ability to pay their registration fees at the time of each shelf takedown. Like operating companies, closed-end funds and BDCs would generally qualify as WKSIs if they have timely filed all reports and other materials required under the Exchange Act during the prior year and have a public float of at least \$700 million.

Amendments to Prospectus Delivery Rules

Under existing Securities Act Rule 172, issuers, brokers and dealers are permitted to satisfy their obligations to deliver a final prospectus under Securities Act Section 10(a) by filing its final prospectus with the SEC within the time required and if other conditions are satisfied. Currently, closed-end funds and BDCs are excluded from this group of issuers. The proposed amendments would remove the exclusion for offerings by closed-end funds and BDCs.

Public Communication Enhancements

In order for closed-end funds and BDCs to achieve parity with the communication rules under the Securities Act applicable to operating companies, the proposed amendments would:

- Permit funds to use "tombstone ads" to publish certain factual information about an issuer or an offering;

- Provide funds with a bright-line time period ending 30 days prior to the filing of a registration statement, during which period they may communicate without risk of violating gun-jumping provisions;
- Permit certain funds to rely on existing Securities Act rules to publish or disseminate certain regularly released factual business information and forward-looking information;
- Permit funds to use a "free writing prospectus" after a registration statement has been filed; and
- Permit funds that are WKSIs to engage at any time in oral and written communications, including the use at any time of a free writing prospectus, subject to the same conditions applicable to other WKSIs.

New Registration Fee Payment for Interval Funds

Under existing rules, closed-end funds that make periodic repurchases of their shares pursuant to Rule 23c-3 of the Investment Company Act ("*interval funds*") are required to pay a registration fee to the SEC at the time of filing of a registration statement, regardless of when or if they sell the securities that are registered. The proposed amendments would permit interval funds to pay their registration fees in the same manner as open-end funds by allowing fees to be paid within 90 days after the fund's fiscal year-end. The proposed rules would also base the fee on the net amount of shares issued, which would take into consideration the amount of shares repurchased by an interval fund during the same period.

Periodic Reporting Requirements

In connection with the above-discussed proposal to allow closed-end funds and BDCs filing short-form registration statements to incorporate by reference information in certain filed and to-be-filed periodic reports, the proposed rules would require such funds to include key information in their annual reports regarding fees and expenses, premiums and discounts, and outstanding senior securities that the funds currently disclose in their prospectuses. Furthermore, the proposed rules would require closed-end funds to provide management's discussion of fund performance in their annual reports to shareholders, BDCs to provide financial highlights in their registration statements and annual reports, and funds filing a short-form registration statement on Form N-2 to disclose material unresolved SEC staff comments.

Current Reporting Requirements

Under existing rules, Exchange Act reporting companies, including BDCs, are required to publicly disclose on Form 8-K

certain specified events and information on a current basis to provide investors and the market with timely information about these events. These events include, among others, new material definitive agreements, quarterly earnings announcements and releases, new direct financial obligations, changes in directors, sales of unregistered equity securities and submissions of matters to a vote of security holders. Under the proposed rules, this requirement would be expanded to apply to closed-end funds. Many closed-end funds already file current reports on Form 8-K voluntarily or pursuant to the rules of the exchanges on which their securities trade. The proposal would harmonize the requirements applicable to closed-end funds and BDCs with those of operating companies. In addition, the proposed rules would amend Form 8-K to (1) add two new reporting items for closed-end funds and BDCs regarding changes to investment objectives or policies and material write-downs of significant investments and (2) tailor the existing reporting requirements and instructions to closed-end funds and BDCs.

How to Comment

The comment period for the proposed rules will be open for 60 days following publication in the Federal Register. Comments may be submitted through the SEC's internet comment form [here](#), by emailing rule-comments@sec.gov, or by mailing paper comments to the SEC at U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090. All submissions should refer to file number S7-03-19.

For More Information

If you would like to discuss any topic covered in this Client Alert, please contact a member of the Investment Management Group or visit us online at chapman.com.

Chapman and Cutler LLP

Attorneys at Law · Focused on Finance®

This document has been prepared by Chapman and Cutler LLP attorneys for informational purposes only. It is general in nature and based on authorities that are subject to change. It is not intended as legal advice. Accordingly, readers should consult with, and seek the advice of, their own counsel with respect to any individual situation that involves the material contained in this document, the application of such material to their specific circumstances, or any questions relating to their own affairs that may be raised by such material.

To the extent that any part of this summary is interpreted to provide tax advice, (i) no taxpayer may rely upon this summary for the purposes of avoiding penalties, (ii) this summary may be interpreted for tax purposes as being prepared in connection with the promotion of the transactions described, and (iii) taxpayers should consult independent tax advisors.

© 2019 Chapman and Cutler LLP. All rights reserved. Attorney Advertising Material.