Simpson Thacher

Registered Funds Alert

January 2019

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The latest edition of Simpson Thacher's Registered Funds Alert discusses observations, trends and predictions for the year ahead, including: the state of the industry; a highly anticipated concept release exploring options for retail investors to have greater access to private company investments; the potential ability of a recent SEC no-action letter to spark reforms regarding the increasingly heavy burdens placed on fund boards; and suggested improvements to the SEC's recent fund of funds rule proposal.

Looking Ahead to 2019

Seismic changes in investor preferences and regulatory requirements are reshaping the landscape of the registered funds space. Potentially disruptive technologies loom on the horizon, and fee pressure and margin compression continue to affect all parts of the industry with no signs of abating. As investors wonder if the 10-year bull market will finally come to an end, investment managers will have to continue to innovate to attract and retain investors in 2019. In these challenges, however, we see some of the clearest opportunities for distinction and growth from managers and areas where regulators can take helpful actions. In this Alert, we explore the state of the industry as we enter 2019 and discuss what trends and themes we expect and hope to see throughout this year.

State of the Industry

The expectations, sophistication and cost-sensitivity of retail investors are all in flux. Investors' willingness to pay fees for market-matching performance has plummeted, as the historic bull market run and rise of exchange-traded funds ("ETFs") has brought low-cost index investing fully to the forefront of retail investing. Of the top 20 registered funds by net inflows in 2018, 13 of them were ETFs, and index funds generally dominate the list.

At the same time they are pursuing lower-cost strategies, investors are expecting more for their money. Notwithstanding the immense fee pressure on the industry, customers are demanding elegant interactions with their portfolios through online portals and smartphone applications and even smart speakers, through which they expect professional investment advice delivered directly to them on demand and in the format that best fits their lifestyles. Investors are now also more interested than ever whether their investment portfolios align with their personal beliefs.

All of this is set against a regulatory backdrop that has seen the SEC undertake significant regulatory reforms that the industry must adopt mid-stride.

How the industry will continue to respond to the changing landscape will largely define the major trends of 2019, and we think there are three main strategies that will be deployed: innovating ways to sell new products, reimagining fee structures, and expansion and consolidation through merger and acquisition activity.

Innovation in Customer Interaction and Products

For investment management firms, reducing friction in the customer experience is a significant part of attracting and retaining new clients. From the moment of account creation through managing tax documentation and other materials, keeping and retaining customers requires adjusting to changing consumer preferences. Millennials, for instance, overwhelmingly prefer to interact with their investment management platform through intuitive smartphone applications and web portals. Platforms that do not provide a smooth customer experience struggle to attract younger clients, while those that excel in those areas are booming.

Artificial intelligence ("AI") has been discussed for many years as a direct investment tool, but the technology may also have promising applications in enhancing the customer experience. Sophisticated investors have used technology that is loosely referred to as AI to interpret massive amounts of data and follow simple algorithmic rules for decades. Historically, its primary use has been geared towards improving investment selection, but now AI is being used to augment the way investment advisers interact with their clients. At least one firm has begun integrating an AI-based customer service enhancement initiative into its platform. The technology works by evaluating communications with clients by analyzing e-mails, text messages and other notes. It then applies machine learning to evaluate other ideas that can be suggested to the client with the aim of improving the overall investing experience.

Similarly, investors may soon be able to get advice from Siri or Alexa. At least one U.S.-based investment management firm is working towards offering investment advice through digital voice assistants ("DVA"). These DVA-based services may advise clients on the amount they need to invest or suggest portfolio allocations based on targets

set by the client. As the ultimate goal of most DVA technologies is to seamlessly replicate interacting with a personal assistant, the regulatory issues regarding licensing and disclosure are complex.

As more of these potentially disruptive technologies come to market, it is likely that regulators will attempt, but struggle, to keep up. There are several potential regulatory issues with the integration of technology into providing advice, and the SEC and other regulators may deem some problematic while others permissible. This could lead to regulatory authorities effectively dictating the winners and losers in the race to bring new products and services to market, potentially increasing the entrepreneurial risk of such developments. Industry participants will have to weigh the advantages of being cutting edge with the uncertainty of looming regulation. Historically, such uncertainty has tended to allow smaller, more nimble advisers to experiment and push the envelope first, and those that do so successfully become prime targets for acquisition as larger investment managers will often acquire firms that have pioneered new technologies. We expect that we will see a marked increase in acquisition activity targeted towards tech-forward investment management firms that have developed scalable advisory tools and technologies for enhancing customer experience.

In addition to improving ways of reaching customers, investment managers will also be looking to respond to shifting customer demands through new product offerings. Technology has ushered in the rise of transparency, and it appears to be here to stay. Retail investors want to know what they are investing in and now have the tools to find out in a few keystrokes. It is no surprise then that the practice of integrating environmental, social and governance (“ESG”) factors into investing has exploded. ESG factors cover a wide spectrum of issues that traditionally are not part of financial analysis. This might include a corporation’s response to climate change, its stance on water management, metrics regarding how effective their health and safety policies are, how sustainable their supply chain is, how they treat their workers, etc. Millennials seem to be more socially aware than prior generations, or at least more interested in congruity between their values and their actions. We expect investment managers that provide options allowing investors to express their own values and to ensure that their savings and investments reflect their preferences (especially if it can be done without compromising on returns) will be in a prime position to capture and retain business in 2019.

Products that offer alternatives to traditional equity funds also appear ripe for expansion in 2019. With the potential for the bull market to come to an end, managers offering private equity options to retail investors may be well-positioned to succeed. Private equity buyout funds have consistently outperformed equity markets, especially so in worse overall economic conditions.[1] Access to such investment strategies would be a boon to retail investors, especially for long-term retirement-focused saving. Traditionally, registered funds have had relatively little exposure to private equity. Among other reasons, the long lock-up periods involved are generally incompatible with funds that have daily liquidity needs, such as traditional mutual funds. With respect to closed-end funds, which are not subject to daily redemption, the potential for growth is limited by the fact that the SEC staff presently takes the position only accredited investors may invest in public closed-end funds that invest more than 15% of their assets in private equity funds.

As we discuss in greater detail later in this Issue, we believe for the private equity trend to really take off among retail investors, regulatory changes would be necessary. Specifically, in 2019 we hope to see the SEC staff adopt the proposal of the Committee on Capital Markets Regulation and reverse its position on applying the accredited investor standard on a look through basis to public closed-end funds that invest more than 15% of the in assets in private equity funds. Chair Clayton has signaled his willingness to explore opportunities for retail investors to gain exposure to private equity, and revisiting this position may be an efficient way to open private equity funds to more retail investors. Alongside the SEC’s modernization proposals (which we also discuss in greater detail later in this

1. Robert S. Harris, Tim Jenkinson and Steven N. Kaplan, How Do Private Equity Investments Perform Compared to Public Equity, 14 J. OF INV. MGEMT. 14, 17 (2016).

Issue), we believe the SEC staff could take major steps in 2019 towards allowing registered funds to offer innovative products to retail investors while simultaneously streamlining their operations.

Reimagining Fee Structures

One of the main drivers of falling fees has been flows into lower-cost funds, primarily illustrated by the outflows from active funds and inflows to passive options. Also contributing to declines have been aggressive fee cuts for passively managed index funds, which in turn have drawn strong inflows relative to more expensive passive options.

The funds winning with respect to fund flows are doing so by leading on cost. As mentioned above, low-cost index funds dominated the list of top 20 U.S. funds by net inflows. The average expense ratio among the top 20 registered funds by net inflows in 2018 was 0.14%, nearly 40 basis points lower than the average registered fund.

Even among the top-tier, low-cost index funds, however, a fee war has raged and resulted in multiple managers resorting to the nuclear option: (ostensibly) no-fee funds. These funds have an expense ratio of zero, no expenses for marketing, and when you buy directly from the manager, there are no transaction fees. One of the hurdles to offering zero-fee funds is creating and maintaining proprietary indices rather than licensing a well-known index like the S&P 500, but now a number of firms are launching proprietary ETF indices allowing them to lower their expense ratios. We expect to see the trend towards low- to no-fees index funds that utilize proprietary indices to continue.

“Even among the top-tier, low-cost index funds, however, a fee war has raged and resulted in multiple managers resorting to the nuclear option: (ostensibly) no-fee funds.”

While it is the broad-based market funds that have gone to this model, the precedent has been set and pressure on this portion of the market will persist. With the advent of zero-commission platforms, some managers are shifting their revenue generation models to securities lending, record-keeping services for 401(k) plans and shareholder servicing fees; changes that are most profitable with significant scale. That trend also looks to continue in 2019, and will continue to drive mergers and acquisitions among the large asset managers seeking the critical scale to compete in the space.

Active funds are also looking to innovate on fee structures through the so-called “fulcrum fee” model. A fulcrum model links fees to fund performance and charges a base fee if a fund does not outperform its benchmark. To the extent a fund does exceed the benchmark, an additional performance fee is assessed. The argument is that variable fee structures will ultimately deliver better net returns to investors and incentivize fund managers to focus on performance rather than fundraising. We have our doubts about these fee structures, and indeed believe that shareholders would be better served by performance fees that only compensate managers for over-performance (compared to fulcrum fees), but nonetheless expect to see more asset managers experiment with this approach in 2019 and beyond given the prohibition on most other performance fees for registered funds.

Growth Through Acquisitions and Consolidation

As we have discussed in a previous Alert, the asset management industry is in a period of increased levels of merger and acquisition activity, and we expect that to continue through 2019 and beyond. Larger investment managers have effectively used their scale to bolster profit margins, while continuing to drive down costs. The gap is only widening between leading and lagging asset management firms, and this trend shows no sign of slowing. We expect the wave of smaller asset manager acquisitions to continue as many struggle to maintain profitability in the face of considering whether to make the significant capital investments in technology and product development to match the expectations of investors. Meanwhile, many larger investment managers will seek strategic acquisitions that will bring new product offerings, investment capabilities or technologies under their umbrellas.

In addition to wholesale mergers or acquisitions, we expect to see a continued uptick in minority stake investments in 2019. Certain businesses that are in adjacent spaces, such as micro-investing, may prove to be attractive targets to traditional asset managers. For instance, a leading U.S.-investment manager recently invested in micro-investing app Acorns with the hopes that it will provide them insight into younger investors. We expect to see an increase in similar transactions throughout 2019.

All of this is occurring against a backdrop of divided control on Capitol Hill and, as of this writing, a potential second government shutdown that may grind the gears of the SEC to a halt again, just weeks after a prolonged shutdown. One prediction we know will come true—2019 will be interesting, if nothing else.

SEC Set to Explore Opening Investments in Private Companies to Retail Investors

Over the past 20 years, the number of publicly listed companies has been cut in half and the public firms that remain are generally older, larger, slower growing and represent a larger portion of market capitalization. Today, there are fewer listed companies than there were in 1976, despite the fact that gross domestic product is three times larger now than it was then. The largest 1% of U.S. public companies represent 29% of total U.S. market capitalization and approximately 140 companies represent more than half of total market capitalization. In part to address the continued erosion of the available opportunity set for public equity investors, Securities and Exchange Commission Chairman Jay Clayton announced in August 2018 that the SEC staff is working on a concept release that will address retail investor access to private companies and the exempt offering framework. We believe it is imperative that the concept release address the ability of retail investors to access private companies through commingled investment vehicles.

> *"The largest 1% of U.S. public companies represent 29% of total U.S. market capitalization and approximately 140 companies represent more than half of total market capitalization."*

Chairman Clayton has acknowledged the dwindling investable universe available to retail investors, stating during his confirmation hearing before the Senate Banking Committee that "our public capital markets are less attractive to business than in the past. As a result, investment opportunities for Main Street investors are more limited." As a result of the shrinking opportunity set in public capital markets and the growth of private markets, individual investors have a limited ability to access the complete U.S. equity market. As many companies wait until they are more mature to go public, the public market offers limited exposure to younger companies with potential for rapid growth, so retail investors lose out on the opportunity for significant growth potential that young companies can offer. Since the public listing peak in 1996, the average public company is 50% older and approximately four times larger than it was 20 years ago. Over the same period, the number of companies in the S&P 500 with annual revenue growth of at least 20% has decreased by half (from 20% of companies to 10% of companies).

Because companies are staying private for longer, by the time of an initial public offering (the first time retail investors are eligible to invest directly), companies have achieved greater scale (both by revenue and market cap), which some commentators argue has a dampening effect on future potential for revenue and returns growth. Private start-up companies are frequently reaching billion-dollar valuations before opening up to the public for investment—as of April 2018 there were 103 privately held U.S. start-ups with valuations of over $1 billion and a total value of $385 billion.

Studies of private equity funds consistently find that private equity returns—net of fees—outperform public market alternatives while providing diversification, lower volatility and protection in times of market stress.[2] Based on an average private fund duration of five years, the outperformance of the most successful private equity funds (e.g., the top 25% of funds) is 7.3% over the S&P 500. To illustrate the issue for Main Street investors, consider that a $10,000 investment in a retirement fund that earned 7% annually from the S&P 500 over 30 years would result in an ending balance of $76,123. Alternatively, if the $10,000 had been invested in a private equity fund that earned 7.3% above the S&P 500 annually, the ending balance would be $551,299.

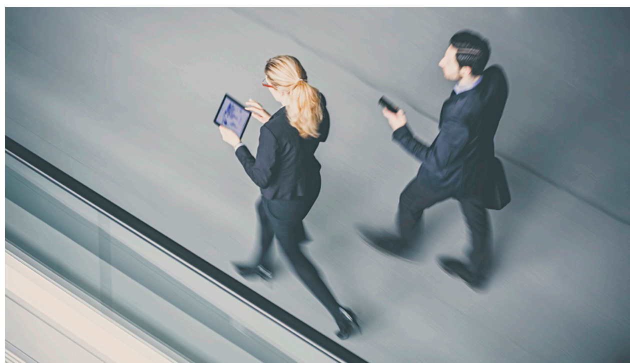
Previously, retail investors could access private equity investments through employer-sponsored retirement accounts. As of January 31, 2018, public defined benefit plans allocated 7.4% of their investments to private equity, which accounted for 35% of the global aggregate capital invested in private equity.[3] However, over the past several decades, employers have embraced defined contribution plans, such as 401(k)s, and shifted away from defined benefit plans. The departure from defined benefits plans is notable in light of evidence that defined benefit plans outperform defined contribution plans. For instance, a Boston College Center for Retirement Research study found that, from 2003 to 2012, private defined benefit plans with more than $100 million of assets outperformed similarly sized private defined contribution plans by 1.5% annually. Defined contribution plans typically do not invest in private equity. Given the strong performance of private equity funds and based on review of the Boston

2. See also David Robinson & Berk Sensoy, Cyclicality, Performance Measurement, and Cash Flow Liquidity in Private Equity, 122 J. Fin. Econ. 251 (2016); Robert Harris et al., Private Equity Performance: What Do We Know?, 69 J of Fin. 1851 (2014).

3. Preqin, Global Private Equity and Venture Capital Report 1, 77 (2018).

College study, the Committee on Capital Markets Regulation concluded that the performance of private equity funds is likely contributing to defined benefit plans' outperformance relative to defined contribution plans.

Chair Clayton has flagged several potential areas of focus for the concept release, including whether rules that limit who can invest in certain offerings should be expanded to focus on the sophistication of an investor, the amount of an investment, or other criteria rather than just the wealth of an investor. We believe registered funds and registered investment advisers should be key components of Chair Clayton's goal to increase access to capital markets and level the playing field for retail investors. In this Alert, we suggest several areas of reform for consideration by the SEC staff.



Expand the Accredited Investor Definition

To invest directly in securities offerings of private companies and private funds, retail investors generally need to be "accredited investors." In addition, retail investors can gain access to investments in private companies through registered funds that invest in hedge funds and private equity funds, but the SEC generally requires that such funds only be offered to accredited investors.

To meet the accredited investor standard, individual investors must have earned at least $200,000 in annual net income in each of the past two years or hold $1 million in net worth, excluding their primary residence. This high qualification hurdle reduces the ability of Main Street retail investors to gain exposure to private companies through hedge funds and private equity funds—a recent Wall Street Journal analysis finds that approximately 87% of U.S. households do not meet the accredited investor standard.

The existing accredited investor standard is based at least in part on the presumption that wealth is the only appropriate proxy for investor sophistication. However, even the SEC has acknowleged that "well informed investors who are not wealthy may be in a position to take on risks that they understand well." One way retail investors can reach the requisite level of financial sophistication to understand the risks of investing in private companies is through expert advice from investment advisers and brokers. In fact, Regulation D indirectly acknowledges that access to expert advice can deem an otherwise unqualified investor de-facto sophisticated so long as the investor is represented by someone who "has knowledge and experience in financial and business matters that he [or she] is capable of evaluating the merits and risks of the prospective investment."[4]

The SEC should consider expanding the definition of "Accredited Investor" to include any investor who is advised on the merits of making a private placement investment by a fiduciary or intermediary that has an obligation to act in the best interests of the investor, such as a registered investment adviser or broker.

Ease or Eliminate Restrictions on Closed-End Fund Access to Private Companies

Unlike mutual funds, which allow for daily redemptions, shareholders in closed-end funds generally have no right to redeem. As a result, closed-end funds are well positioned to invest in illiquid assets, such as private companies and private equity funds.

Certain closed-end funds registered under the Investment Company Act invest a significant portion (more than 15%) of their assets in private equity funds and other types of private funds. However, in disclosure comment letters to these funds the SEC staff has indicated its view that only accredited investors may invest in a public closed-end fund that invests more than 15% of its assets in Section 3(c)(7) funds.[5] The SEC has not stated the legal or policy basis for this position. The argument that Main Street investors should be excluded because they could not invest directly in such funds is less convincing when one considers that registered funds often invest in securities in which Main Street investors cannot directly, such as 144A offerings and other private placement transactions. Because the SEC staff's blessing is required for such registered funds of funds' registration statements to become effective, the industry has had no choice but to acquiesce to this requirement.

4. Regulation D limits the number of non-accredited, financially sophisticated investors who may invest in an offering to no more than 35. An offering to non-accredited investors is also subject to enhanced disclosure requirements.

5. See also Wildermuth Endowment Strategy Fund, SEC Comment Letter (October 11, 2013); Cross Shore Discovery Fund, SEC Comment Response Letter, (Sept. 17, 2015); Resource Real Estate Diversified Income Fund, SEC Comment Letter (Oct. 19, 2012); Oxford Lane Capital Corp., SEC Comment Response Letter, (Aug. 17, 2015).

The SEC and its staff should consider allowing retail investors to invest in public closed-end funds that invest more than 15% of their assets in private equity funds (and/or should expand the definition of "accredited investor" as proposed above). Public closed-end funds are subject to extensive disclosure requirements regarding their allocations to specific private equity funds and fees associated with these investments. A public fund of private funds offers retail investors the opportunity to gain indirect access to attractive private fund opportunities that are otherwise only available to institutional investors, and public fund sponsors can offer expertise in selecting and negotiating private fund investments. As discussed above, retail investors need access to private companies to obtain adequate diversification and superior returns and commingled investment vehicles managed by investment advisers who owe fiduciary duties to such vehicles is one potential source of such access.

Easing Restrictions on Affiliated Funds of Private Equity Funds

In addition to the restrictions on closed-end funds of private funds discussed above, the affiliated transaction restrictions of the 1940 Act currently prevent a sponsor from managing a registered fund that invests in private funds managed by the same sponsor. Some registered funds (currently available only to accredited investors) focus their investments on private funds of a single sponsor, but the registered funds are managed by a third party unaffiliated with the private fund sponsor. However, the unaffiliated investment advisers to such funds each charge an annual management fee in excess of 1% even though the investment strategies contemplate that each fund will invest at least 80% of its assets in funds of a specific private equity firms.

A third-party adviser is one way to protect against conflicts of interest but the SEC should consider alternative options to permit affiliated funds of funds, subject to certain limitations. Investors will benefit by having access to a registered fund of private funds managed by an affiliated investment adviser that has the greatest knowledge of the investment strategies and investment characteristics of the underlying private funds. The SEC can address affiliated transaction concerns by imposing certain limitations, such as:

- The registered fund's board of directors will only approve fund-level fees for services that are in addition to and not duplicative of services at the underlying fund level;
- The registered fund will not own more than 25% of any underlying closed-end funds;
- The registered fund will not own more than 25% of any underlying open-end funds and will be restricted from seeding open-end funds;
- The registered fund will not invest in other funds of funds and will not invest more than 40% of its assets in a single fund;
- The registered fund will vote its interests in any underlying fund in the same proportion as the vote of all other shareholders in a particular underlying fund; and
- The registered fund will receive most favored nation treatment with respect to all investments in underlying funds.

The SEC should consider providing greater flexibility to permit affiliated "fund-of-private fund" arrangements similar to fund-of-fund arrangements involving mutual funds permitted under Section 12(d)(1)(G) of the Investment Company Act and Rule 12d1-2 thereunder (as discussed later in this Alert, the SEC recently proposed Rule 12d1-4 which would rescind Rule 12d1-2 and related exemptive orders).

Rationale of Recent No-Action Letter, If Extended to Other Areas, Could Go a Long Way Toward Reducing Unnecessary Burdens on Fund Boards

Boards of registered funds serve a critical "watchdog" function for shareholders, but the growth of responsibilities given to directors, driven largely by SEC rulemaking, has made it increasingly difficult for board members to focus on their core function.

After a keynote address by Dalia Blass, Director of the SEC's Division of Investment Management, at the 2018 Investment Company Institute Mutual Funds and Investment Management Conference, participants in the mutual fund industry were eager to see whether her goal of "understanding where [the fund] board oversight role is most valuable" would translate into meaningful adjustments to the burdens placed on fund boards. On October 12, 2018, boards received some initial relief when the staff of the SEC's Division of Investment Management issued a no-action letter to the Independent Directors Council confirming that the Division would not recommend an enforcement action if a board relies on reports from a fund's Chief Compliance Officer that certain transactions were effected in compliance with the board's procedures for such transactions, in lieu of the board being required to review such transactions and make the compliance determination itself (the "IDC No-Action Letter").

The IDC No-Action Letter was a welcome first step to improve board efficiency, but there remain opportunities for the Staff to modernize further board responsibilities while still protecting shareholder interests. In this Alert, we provide background on the SEC's Board Outreach Initiative, which ultimately led to the IDC No-Action Letter. We then discuss an additional area ripe for board oversight reform: co-investment programs.

The SEC's Board Outreach Initiative and the IDC No-Action Letter

The effort to modernize board duties is not a new endeavor at the SEC. During her address, Ms. Blass referred to the "Board Outreach Initiative," a program that has existed for over ten years. At his keynote address at the 2007 Investment Company Directors Conference, the then-Director of the SEC's Division of Investment Management, introduced the initiative as a way for the SEC to help boards perform their duties and continue to add value for shareholders. As part of the initiative, the SEC solicited direct input from boards, including by meeting with boards at their regularly-scheduled meetings. Despite the apparent support for the initiative, the financial crisis and related Dodd-Frank Act and Financial Stability Oversight Council-driven rule-making initiatives that followed the crisis took the focus and momentum away from the Board Outreach Initiative.

In October 2017, the IDC wrote a letter to Ms. Blass requesting that the Division renew focus on modernizing board responsibilities. In that letter, the IDC noted that the earlier initiative had not resulted in meaningful recommendations from the SEC, and that the regulatory landscape had continued to change and additional responsibilities placed on boards over the past decade. The IDC urged the Division to take a fresh, comprehensive look at board duties in light of the current state of the industry. The IDC provided a number of preliminary recommendations, including changes to the three rules that were subsequently addressed in the IDC No-Action Letter. At her 2018 keynote address, Ms. Blass indicated the Staff had met with boards and groups of independent directors in an attempt to restart the initiative and intended to prioritize these efforts going forward.

> *"The IDC urged the Division to take a fresh, comprehensive look at board duties in light of the current state of the industry."*

The IDC No-Action Letter is the initial result of these efforts. In the letter, the Staff confirmed it would not recommend an enforcement action if, in lieu of a board making the required determinations that any transactions with affiliates covered under Rules 10f-3(c), 17a-7(e)(3) and 17e-1(b)(3) of the Investment Company Act of 1940 were compliance with board-approved policies and procedures adopted pursuant to such rules, a board were to instead rely on a report from the CCO to that effect. The SEC recognized the adoption of Rule 38a-1 under the 1940 Act reflected the SEC's view that boards should *oversee* compliance matters instead of being involved in the day-to-day administration of a fund's compliance program. The Staff reiterated that the board's oversight role with respect to a fund's overall compliance program remains unchanged by the IDC No-Action Letter.

The IDC No-Action Letter signals a notable shift in the Division's view on a board's ability to delegate additional responsibilities to a CCO to reduce the burden on the board. The SEC previously issued a letter to the IDC and Mutual Fund Directors Forum in which it clarified that a board may rely on a CCO's report regarding the transactions covered by the rules addressed in the IDC No-Action Letter, but the board was still required to make compliance determinations under the rules. Under the IDC No-Action Letter, a board is no longer required to make such determinations.

Co-Investment Programs

We believe a logical next step in light of the IDC No-Action Letter and the SEC's reinvigorated effort to improve board efficiency is for the Staff

to take a fresh look at boards' roles with respect to co-investment programs. The purpose of the conditions in co-investment exemptive relief applications is to mitigate conflicts of interest. In the way that the approval of Apollo Investment Corporation's co-investment application signaled an attempt by the Staff to provide more practical exemptive relief and to take into account the realities of the asset management industry, we believe the next wave of exemptive relief applications should go a step further and provide an alternative to the current condition that boards must make certain findings regarding a potential co-investment transaction.

In our last Alert, we described the evolution of co-investment exemptive orders that have been granted by the SEC. In that Alert, we noted that renewed innovation in co-investment programs began with the order granted to Apollo in 2016. Although Apollo's relief was a successful (albeit lengthy) negotiation between the Staff and Apollo, the relief issued to Apollo and subsequent applicants still requires that the board approve, at minimum, a registered fund's participation in the initial co-investment transaction in a given issuer based on written information provided by the adviser. In approving a funds participation in a co-investment transaction, the board is presumably not asked to evaluate an investment on the merits, but instead must determine that:

- (i) the terms of the transaction are reasonable and fair to the fund and its shareholders and do not involve overreaching;
- (ii) the co-investment transaction is consistent with the interests of shareholders and the participating fund's current objectives and strategies;
- (iii) the investment by other funds would not disadvantage the participating fund and the participating fund's participation would not be on a different basis or less advantageous than that of any other fund(s); and
- (iv) the proposed investment will not involve compensation, renumeration or direct or indirect financial benefit to the adviser, any other fund, the affiliated funds or any of their affiliated persons. The board is also required to approve a fund's participation in certain follow-on investments and disposition opportunities.

The IDC No-Action Letter raises considerations that also are present in co-investment programs. The IDC No-Action Letter did not seek to change a board's responsibility to adopt procedures under the rules; instead, the relief allows a board to focus on its oversight role by not requiring it to determine affirmatively that each transaction was effected in compliance with board-established procedures. Similar to the rules that require a board, including the majority of independent directors, to adopt procedures that are reasonably designed to provide that transactions comply with the affiliated transaction requirements under the rules, a co-investment exemptive order require the board to oversee the procedures that ensure compliance with the terms and conditions of the exemptive order. However, the exemptive orders also require the board to make the determinations noted above for every single co-investment in which a registered fund proposes to participate in advance of the investment.

We believe the board's role with respect to co-investment transactions should be focused on overseeing the review, approval and allocation process for these transactions. The board should not be required to make the transaction-specific determinations required by current exemptive orders. These determinations are more appropriately within the purview of the adviser's investment and compliance personnel and it is not clear that any meaningful additional protections are gained by the board signing off on individual transactions. In practice, these potential co-investment transactions often come up between board meetings and on expedited timelines, causing logistical issues for both the board and the participating funds.

We believe that board reporting from the adviser on a quarterly basis should replace real-time board involvement. This approach aligns with the manner in which the board oversees how an adviser handles potential co-investment transactions in which a registered fund declines to participate. In addition, co-investment programs already require that the CCO oversee compliance of the program and prepare an annual report to the board regarding each fund's compliance with the terms and conditions of the exemptive relief order. Similar to the IDC No-Action Letter, the board should be able to rely on certifications from both the adviser and the CCO stating that each co-investment transaction met the four mandatory conditions before a registered fund participated in the transaction. This change would allow the board to enhance its oversight function, as the board would receive the same level of information it does currently, just in the context of a quarterly board meeting during which any issues could be addressed face-to-face with the adviser. Fund shareholders will be sufficiently protected by the CCO's and adviser's fiduciary responsibilities and expertise, guided by the policies and procedures

approved by the board and the board's general oversight. We believe this change is aligned with spirit of Rule 38a-1.

The IDC No-Action Letter and the revival of the Board Outreach Initiative were welcome developments in the effort among industry participants to streamline fund board responsibilities. We believe the next area of focus for the Staff should be co-investment programs. Co-investment program changes could come through the exemptive relief process or through the no-action process with the Staff taking a position that it would not recommend enforcement if a fund board were to rely on certifications from the adviser and the CCO in lieu of making the four determinations in an exemptive order. Simpson Thacher will be actively monitoring this area and will address any developments in future Alerts.

The Proposed Fund of Funds Rule—A Good First Step That Merits Further Consideration

The SEC recently proposed new Rule 12d1-4 under the 1940 Act that, if adopted, would provide an exemption for fund of funds arrangements where registered funds and business development companies (collectively, "regulated funds") acquire shares of other regulated funds in excess of the statutory 1940 Act limits. This article provides background on the fund of funds restrictions in the 1940 Act, current exemptions to these general prohibitions and an overview of the requirements of the proposed rule. The article then examines potential adverse or unintended consequences of the proposed rule and suggests potential revisions for the SEC staff to consider prior to adopting a final rule.

Background

Section 12(d)(1) of the 1940 Act restricts the ability of a regulated fund (an "acquiring fund") to invest in other funds ("acquired funds"). There are three key restrictions that apply each time an acquiring fund purchases shares of an acquired fund, commonly referred to as the 3%/5%/10% restrictions (together, the "12(d)(1) Limits"):

1. an acquiring fund cannot own more than 3% of the total outstanding voting stock of a single acquired fund (note: the 3% limit also applies when private funds relying on the exceptions in Sections 3(c)(1) and 3(c)(7) of the 1940 Act acquire shares of regulated funds);
2. an acquiring fund cannot invest more than 5% of the value of its total assets in a single acquired fund; and
3. an acquiring fund cannot, in the aggregate, invest more than 10% of its total assets in acquired funds.

The 1940 Act and the rules thereunder include certain exemptions from the 12(d)(1) Limits for master-feeder arrangements, affiliated fund of funds arrangements, investments in money market funds, and acquisitions of less than 3% of an acquired fund's securities in the aggregate by a regulated fund and all affiliated persons of such regulated fund. The SEC has also issued numerous exemptive orders (the "Existing Orders") that allow certain regulated funds to invest in shares of other regulated funds in excess of the 12(d)(1) Limits, subject to certain conditions and the execution of a participation agreement between the acquiring fund and the acquired fund. Under these participation agreements, an acquired fund agrees to allow the acquiring fund to acquire more than 3% of its shares in reliance on the order and each fund agrees to comply with the applicable conditions of the order. As is often the case with exemptive orders, the conditions contained in the various Existing Orders are generally similar, but not identical.

Overview of the Proposed Rule

The proposed rule would allow a regulated fund to acquire shares of another regulated fund in excess of the 12(d)(1) Limits, subject to the following conditions:

- *No private funds may rely on the proposed rule.* The rule would only be available for investments by regulated funds. Private funds could not rely

on the rule as proposed, and thus would still be restricted to the 3% limit described above.

- *No controlling stake*. An acquiring fund and its advisory group will not control (individually or in the aggregate) an acquired fund. Under the 1940 Act, control is presumed when a person (or in this case, a group) beneficially owns, directly or through one of more controlled companies, more than 25% of another person's voting securities. "Advisory group" refers to an acquiring fund's investment adviser, sub-adviser or depositor (*i.e.*, sponsor), and any person controlling, controlled by, or under common control with such investment adviser, sub-adviser or depositor (including other funds managed by the sponsor).

- *Acquiring funds must either mirror vote or pass-through vote*. If an acquiring fund and its advisory group hold more than 3% of an acquired fund's outstanding voting securities in the aggregate, each holder will either mirror vote its acquired fund shares in the same proportion as the vote of all other shareholders or seek voting instructions from its shareholders. The mechanics of this proposal are identical to the 1940 Act voting provisions for master-feeder funds.

- *Redemptions limited to 3% per any 30-day period*. When an acquiring fund holds more than 3% of an acquired fund's outstanding voting securities, such acquiring fund may not redeem more than 3% of the acquired fund's outstanding voting securities during any 30-day period.

- *Adviser must undertake a periodic evaluation*. Before investing in an acquired fund in reliance on the rule, and no less frequently than annually thereafter, the acquiring fund's investment adviser must evaluate the complexity of the structure and the aggregate fees associated with the acquiring fund's investment in the acquired fund, and find that it is in the best interest of the acquiring fund to invest in the acquired fund. The investment adviser of the acquiring fund must report its findings to the fund's board.

- *Restrictions on complex fund of fund structures*. If a regulated fund intends to be (or at times may be) an acquiring fund for purposes of the rule, it must disclose that intent in its registration statement. No acquiring fund may acquire shares of another regulated fund in excess of the 12(d)(1) Limits if the prospective acquired fund has disclosed that it may be an acquiring fund under the rule. Under the proposed rule, an acquired fund is also prohibited from acquiring shares of other funds (including private funds even though there is otherwise no stattutory basis for limiting investments in private funds) in excess of the 12(d)(1) Limits except for certain limited circumstances, including master-feeder arrangements, investments in money market funds for cash management purposes, investments in wholly owned subsidiaries and interfund borrowing and lending transactions pursuant to a SEC exemptive order.

- *Additional recordkeeping requirements*. The acquiring fund must maintain and preserve for not less than five years a written record of the investment adviser's finding that the investment is in the best interest of the acquiring fund.

Key Issues the SEC Should Reconsider

There are a number of aspects of the proposed rule that should be reconsidered before the SEC adopts a final rule. Certain of these considerations are discussed below.

Private funds should be allowed to qualify as acquiring funds under the rule when investing in ETFs and other open-end funds

Private funds cannot rely on the proposed rule to invest in ETFs and other open-end funds. The SEC should reconsider whether to allow private funds to acquire interests in ETFs and other open-end funds in excess of the 12(d)(1) Limits under the final rule.

While there are some key additional factors to be considered in permitting private funds to rely on the rule, as discussed in further detail below it would not appear to be impractical to address those key considerations in a revised final rule. If the changes proposed below are implemented, it would appear that allowing private funds to invest in regulated funds in excess of the 12(d)(1) Limits in accordance with the conditions of the rule would not present any additional meaningful risks than those associated

with a regulated fund engaging in the same activity. Certain concerns, such as large-scale redemption requests by acquiring funds, are less relevant when a private fund is an acquiring fund since most private funds do not offer daily liquidity to their investors. Like regulated funds, private funds also invest in ETFs and other regulated funds to gain market exposures. So long as a private fund complies with the conditions of the rule, there is no apparent reason to treat investments by private funds in ETFs and other open-end funds differently under the rule.

The proposing release explains that private funds were omitted from the types of funds that can rely on the rule because private funds (i) do not make annual reports on Form N-CEN, (ii) do not report acquired fund holdings on Form N-PORT and (iii) are not subject to the recordkeeping requirements of the 1940 Act. These concerns should not preclude private funds from relying on the rule as acquiring funds because the rule could be revised to require substantially similar reporting and recordkeeping for private funds. For example:

- (i) the investment adviser to the private fund could be required to make the same disclosures by adding questions to Form ADV Part 1 that correspond to the questions in Form NCEN,
- (ii) private funds that rely on the rule could be required to submit a confidential monthly report of acquired fund holdings to the SEC that aligns with the information on Form N-PORT or similar reporting could be added to Form PF and
- (iii) the Advisers Act recordkeeping rule could be amended to require investment advisers to private funds that rely on the rule to maintain the records that will be required of regulated funds under the 1940 Act.

Although private fund managers may object to this increased level of required reporting, it is not unreasonable that the ability to rely on an exemptive rule would require a certain amount of concomitant burden on any party that avails itself of the benefits of the rule.

The rule should be revised to include appropriate protections for closed-end funds and BDCs

The rule poses serious concerns for closed-end funds and BDCs in light of the trend for certain activists to form multiple funds to invest in listed closed-end funds and BDCs to seek short-term actions that may not be consistent with the best interests of long-term investors. In particular, the option to pass-through the vote to acquiring fund investors could be abused by acquiring funds managed by activist investors. For example, an activist investor could form a closely held regulated fund to make activist investments in closed-end funds or BDCs. Investors in such funds would be likely to vote in a manner that is consistent with the activist's interest—but may be inconsistent with the best interests of the acquired fund's long-term investors. To protect closed-end funds and BDCs, the rule should be revised to require mirror voting if an acquiring fund managed by a different advisory group holds more than 3% of an acquired fund's shares. Acquiring funds managed by the same advisory group could have the option of mirror voting or pass-through voting.

Allowing private funds to invest in closed-end funds and BDCs in reliance on the rule as proposed would not be in the best interests of long-term investors. If the voting provisions of the rule are revised to require mirror voting when investing in a closed-end fund or BDC, however, then a private fund should not be precluded from relying on the rule to invest in closed-end funds and BDCs. This approach would prevent activist private fund managers from abusing the rule while allowing private funds to gain desired investment exposures through investments in closed-end funds and BDCs.

Acquired funds should be allowed to screen certain acquiring funds

Existing Orders require an acquiring fund and an acquired fund to enter into a participation agreement prior to an acquisition of acquired fund shares that exceeds the 12(d)(1) Limits. While this requirement ensures that each party is contractually obligated to comply with the conditions of the applicable Existing Order, it also allows an acquired fund to screen prospective acquiring funds—i.e., if the acquired fund declines to enter into the participation agreement, the acquiring fund cannot invest in excess of the 12(d)(1) Limits. We anticipate that the removal of the participation agreement requirement will be a welcome development, but the elimination of a mechanism to screen prospective acquiring funds may have adverse consequences for certain acquired funds. For example, if the acquired fund is listed on a stock exchange, or if the acquiring fund invests through an omnibus account, then under the proposed rule the acquired fund may not have the opportunity to reject an investment by an acquiring fund before such investment exceeds the Section 12(d)(1) Limits. Closed-end funds and BDCs may wish to screen prospective acquiring funds to prevent activists from investing in reliance on the rule. Open-end funds may wish to screen investors to manage capacity constraints and redemption risk.

The SEC should consider these potential adverse consequences before finalizing the rule.

A key issue to reconsider is the 3% redemption limit in any 30-day period, which would impose severe limitations on the utility of the rule

The rule condition limiting redemptions to not more than 3% of the acquired fund's total outstanding shares during any 30-day period is not a condition of Existing Orders. The SEC has indicated that the proposed redemption limit is designed to provide a check against the influence that an acquiring fund can have on an acquired fund through the threat of large-scale redemptions. The SEC proposed a mandatory limit that prohibits redemptions above a threshold percentage, rather than a permissive limit that would be at the acquired fund's discretion similar to section 12(d)(1)(F) of the 1940 Act, because the SEC believes an acquiring fund could influence an acquired fund to eliminate (or never establish) a permissive limit on redemptions.

The proposed redemption limit has the potential to adversely affect acquiring fund liquidity and may inhibit current portfolio management techniques—for example, this condition may prevent an acquiring fund from optimally rebalancing its portfolio. We question the need for the redemption limit, especially since it is not a condition of the Existing Orders. We anticipate that the SEC will be presented with alternatives to the 3% redemption limit. For example, some commenters may suggest a higher threshold percentage, relief that would permit the acquired fund to delay redemption payments beyond seven days under certain circumstances (rather than simply prohibiting such redemption), and/or longer notice periods for acquiring funds to redeem a certain percentage of an acquired fund's shares.

> *"We question the need for the redemption limit, especially since it is not a condition of the Existing Orders."*

If the final rule includes a redemption limit, the rule should specify that such investments by acquiring funds will not be deemed illiquid for purposes of the liquidity rule

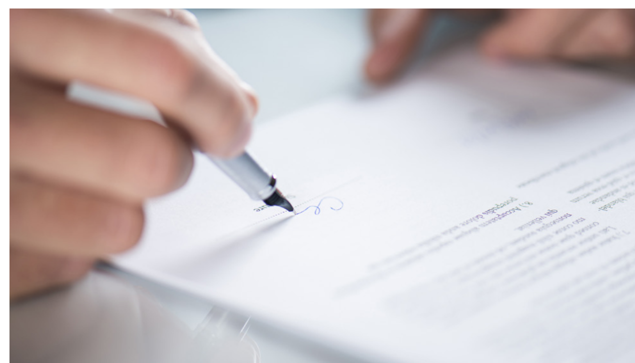
The SEC states in the release that an open-end acquiring fund that relies on the rule should take the 3% redemption limitation into account when classifying its investment in the acquired fund as part of its liquidity risk management program pursuant to Rule 22e-4. In effect, the redemption limit would prevent an acquiring fund from disposing of more than 3% of the acquired fund's shares in seven calendar days or less. If a redemption limit is included in the final rule, the rule should specify that (i) an investment made in reliance on the rule is liquid for purposes of the liquidity rule's 15% illiquid investments limit and (ii) the rule's redemption limit should only be considered for purposes of the liquidity rule's classification requirement .

The rule should not unduly limit the use of efficient portfolio management techniques by acquired funds, such as investments in ETFs

The rule prohibits investments by an acquired fund in other funds, subject to certain limited exceptions that are generally consistent with Existing Orders. As proposed, however, the rule would prohibit portfolio management techniques where an acquired fund seeks to invest in ETFs or other funds to efficiently invest large subscriptions into the fund or to gain investment exposures to certain asset classes. To ensure portfolio management decisions are made in the best interests of acquired fund investors, the final rule should allow acquired funds to invest a portion of their assets in ETFs or other funds for these purposes.

Next Steps

The proposed rule is a necessary step to seek to harmonize the 1940 Act regime for fund of funds investments and to free up SEC staff resources that are otherwise spent reviewing exemptive applications for similar relief. It is likely, however, that the proposal draws significant and wide-ranging comments from the industry. The end of the rule's comment period is not yet known because the proposing release has not been published in the Federal Register due to the partial shutdown of the federal government. The comment period will end 90 days after the proposing release is published. Simpson Thacher will be monitoring developments regarding the proposed rule, which will be addressed in future Alerts.



M&A Transactions

Acquiror	Acquired or Target Company	Type of Transaction and Status
BC Partners Advisors L.P., a leading international investment firm with over $24 billion of AUM across private equity, private credit and real estate strategies	**KCAP Financial, Inc.**, a publicly traded, internally managed business development company	Externalization of management, whereby an affiliate of BC Partners will become the manager of KCAP, KCAP stockholders will receive a cash payment from BC Partners of $25 million, BC Partners will contribute up to 100% of its incentive fees earned, if necessary, to enable KCAP to achieve net investment income of $0.40 per share for the one-year period after closing and BC Partners will use up to $10 million of incentive fees earned to purchase newly issued shares of KCAP stock in the two-year period after closing
Brown Advisory, Inc., an investment and strategic advisory firm with approximately $67 billion in client assets	**Signature Family Wealth Advisors**, a registered investment adviser with approximately $4.3 billion in client assets	Acquisition (terms not disclosed)
Citizens Financial Group, Inc., a financial institution with approximately $158.6 billion in assets	**Clarfeld Financial Advisors, LLC**, a wealth management firm with approximately $6.6 billion in AUM and approximately $900 in assets under administration	Acquisition (terms not disclosed)
Dyal Capital Partners, a private equity and venture capital firm with approximately $14 billion in AUM, and a division of Neuberger Berman Group	**Bridgepoint Capital**, a London-based private equity firm that has approximately €28.2 billion of committed funds and €18 billion in AUM	Acquisition of a minority interest, between 15% and 20%, for receipt of a proportion of Bridgepoint's dividends and carried interest (terms not disclosed)
EB Safe, LLC, subsidiary of **Emigrant Bank**, a privately-held bank specializing in advising financial institutions	**Fiduciary Network, LLC**, an RIA aggregator with approximately $40 billion in AUM	Acquisition; EB Safe will consolidate 100% ownership of Fiduciary by exercise its right of first refusal to acquire the remaining 25% stake in Fiduciary not already owned (terms not disclosed)
Generational Capital LLC, a part of Generational Group that specializes in mergers and acquisitions advisory services	**Talis Advisors**, a registered investment adviser	Acquisition of majority interest (terms not disclosed)
Genstar Capital, a private equity firm with approximately $10 billion in AUM	**Cetera Financial Group**, a network of nearly 8,000 financial advisors	Acquisition of majority interest (terms not disclosed)

M&A Transactions *(continued)*

Acquiror	Acquired or Target Company	Type of Transaction and Status
Goldman Sachs Asset Management, an asset manager whose Alternative Investment & Manager Selection Group has more than $200 billion AUM	**Harvest Partners**, a private equity investment firm	Acquisition of 15% interest (terms not disclosed)
Goldman Sachs Asset Management, an asset manager whose Consumer and Investment Division that has approximately $1.5 trillion assets under supervision	**Rocaton Investment Advisors**, an investment consulting firm that has more than $600 billion in assets under advisement	Acquisition (terms not disclosed)
iM Global Partner, an investment and development platform, having approximately $30.4 billion combined AUM with partner asset managers Polen Capital, Dolan McEniry Capital, Sirios Capital and Dynamic Beta. iM Global Partner represents approximately $7.6 billion AUM in proportion to its participations	**Dynamic Beta investments (previously branded Beachhead Capital)**, a hedge fund advisory firm	Acquisition of 45% interest (terms not disclosed)
Invesco Ltd., an independent investment management firm with approximately $888 billion in AUM	**OppenheimerFunds, Inc.**, a global asset manager with over $246 billion in AUM	Acquisition for total consideration of approximately $5.7 billion, including Massachusetts Mutual Life Insurance Company, the current parent company of OppenheimerFunds, receiving approximately a 15.5% stake in Invesco
Kovitz Investment Group, an investment manager, which is part of Focus Financial Partners	**AFAM Capital**, an investment management firm	Acquisition (terms not disclosed)
Kudu Investment Management, LLC ("Kudu"), a registered investment adviser	**Bingham, Osborn & Scarborough, LLC ("BOS")**, a wealth management firm with approximately $4.7 billion in AUM	Acquisition of minority interest of BOS; the terms include that BOS will buy back its majority stake from Boston Private Financial Holdings, Inc. and BOS will own approximately 68% and Kudu will own 32% of BOS. Boston Private will receive approximately $21 million of cash at closing and an eight year revenue share (terms not disclosed)
LibreMax Intermediate Holdings, LP, an asset management firm with approximately $2.9 billion in AUM	**KCAP Financial, Inc.**'s wholly owned subsidiaries, **Katonah Debt Advisors, Trimaran Advisors, L.L.C.**, ("Trimaran Advisors") and **Trimaran Advisors Management, L.L.C.**; Trimaran Advisors has approximately $3 billion in AUM	Acquisition for $37.9 million in cash

M&A Transactions *(continued)*

Acquiror	Acquired or Target Company	Type of Transaction and Status
Mariner Wealth Advisors, a wealth advisory firm with more than $23 billion in client assets under advisement	**Patriot Wealth Management Inc.**, a financial management firm and RIA with approximately $792.84 million in AUM and approximately $1.86 billion in locally managed assets	Acquisition (terms not disclosed)
Markel Corporation, a financial holding company	**Nephila Holdings Limited**, an investment manager with approximately $12.3 billion AUM	Acquisition of all outstanding shares with financing through cash balances on hand (terms not disclosed)
Mercer Advisors Inc., an RIA with approximately $15 billion in AUM	**Beacon Wealth Management**, a wealth management firm with approximately $230 million in AUM	Acquisition (terms not disclosed)
Mercer Advisors Inc., an RIA with approximately $15 billion in AUM	**Bell Wealth Management**, a wealth management firm with approximately $200 million in AUM	Acquisition (terms not disclosed)
Mercer Advisors Inc., an RIA with approximately $15 billion in AUM	**Sigma Investment Management Company**, a wealth management firm with approximately $500 million in AUM	Acquisition (terms not disclosed)
Natixis Investment Managers, an asset management firm with more than $1 trillion in AUM	**WCM Investment Management**, an investment management firm with approximately $29 billion in AUM	Acquisition of 24.9% equity interest and long-term exclusive global distribution agreement (terms not disclosed)
Neuberger Berman, an investment manager with approximately $315 billion in AUM	**Cartesian Re**, an insurance-linked securities manager and **Iris Re**, an affiliate of Cartesian Re, with combined AUM of more than $1 billion	Acquisition in which Cartesian Re will rebrand as NB Insurance-Linked Strategies and Iris Re will rebrand as NB Reinsurance (terms not disclosed)
PIMCO, a fixed income investment manager owned by Allianz SE	**Gurtin Municipal Bond Management**, an asset manager	Acquisition (terms not disclosed)
Pretium Partners, LLC, an alternative asset management firm with more than $10 billion AUM	**Selene Holdings LLC**, the parent company of SelecTitle, New Diligence Advisors LLC and Selene Finance LP, which provides residential mortgage and loan services	Acquisition using funds managed by Oaktree Capital Management, L.P. and Ranieri Partners LLC. (terms not disclosed)
Private Ocean Wealth Management, a wealth management firm with more than $1.5 billion in AUM	**Mosaic Financial Partners, Inc.**, a registered investment adviser with approximately $620 million in AUM	Acquisition (terms not disclosed)

M&A Transactions *(continued)*

Acquiror	Acquired or Target Company	Type of Transaction and Status
Robert W. Baird & Co., an asset and wealth management firm with more than $200 billion in client assets	**Hillary Lyons and Hillary Lyons Trust Company**, a wealth and asset management firm with more than $50 billion in client assets	Acquisition (terms not disclosed)
Rockefeller Capital Management L.P., financial advisory firm with approximately $18.6 billion in AUM	**Greer Anderson Capital LLC**, a private investment management firm	Acquisition (terms not disclosed)
Sanctuary Wealth Partners, a wealth manager and a division of the Noyes Group	**Winthrop Capital Management**, a registered investment adviser with almost $1 billion AUM	Acquisition (terms not disclosed)
Sequoia Financial Group, a wealth management firm with approximately $4.1 billion in AUM	**LJPR Financial Advisors**, a fee-only advisory firm with approximately $776 million in AUM	Acquisition; the terms include both equity and cash, and no private equity or debt (terms not disclosed)
Stone Point Capital LLC, a private equity firm with approximately $19 billion in committed capital	**Rialto Capital Management LLC**, an asset management segment of Lennar Corporation	Acquisition through payment of $340 million in cash at closing to Lennar Corporation, the parent company. The cash to pay for the acquisition will come from Stone Point's $5.5 billion fund, Trident VII. Lennar will retain its Rialto's Mortgage Finance business and approximately $294 million in fund investments, along with its carried interests in various Rialto funds, as well as investments in other legacy Rialto balance sheet assets
Sun Life Financial Inc., financial services organization with approximately $984 billion AUM	**GreenOak Real Estate**, a real estate investment firm with approximately $11 billion AUM	Merger of the Sun Life Financial North American property management firm Bentall Kennedy with GreenOak Real Estate in which Sun Life Financial will acquire a majority stake in the combined entity named Bentall GreenOak. Sun Life will contribute its interest in Bentall Kennedy and pay GreenOak shareholders $146 million in cash in exchange for a 56% interest in the combined Bentall GreenOak entity, with GreenOak shareholders holding the remaining interest. Sun Life will have an option to acquire the remaining interest in Bentall GreenOak approximately seven years from the closing. Sun Life Financial also will be acquiring the right to a portion of the GreenOak shareholders' share of Bentall GreenOak net income in exchange for a fixed amount to be paid in quarterly installments. This will result in Sun Life Financial having the rights to approximately 90% of the Bentall GreenOak earnings prior to the Company exercising its option to increase its ownership level. The transaction will be financed through surplus cash

M&A Transactions *(continued)*

Acquiror	Acquired or Target Company	Type of Transaction and Status
The Mather Group, a wealth management firm with approximately $1.8 billion in AUM	**Berman Investment Advisors**, a financial planning firm with more than $1 billion in AUM	Acquisition (terms not disclosed)
TK Partners, a consortium of institutional investors formed to acquire Savanna, founded by Turnbridge Investment Partners, an affiliate of advisory firm Hodes Weill & Associates, LP and Seward & Kissel Client, Kudu Investment Management, LLC	**Savanna**, a real estate investment fund manager and developer that has invested more the $4 billion since 1992	Acquisition of minority interest (terms not disclosed)
TPG Sixth Street Partners (“TPG”), a credit platform with approximately $27 billion AUM **Dyal Capital Partner (“Dyal”)**, a private equity and venture capital firm with approximately $14 billion in AUM, and a division of Neuberger Berman Group	**Halycon Capital Management**, an investment management firm with approximately $10 billion in AUM	Acquisition by TPG of a new minority interest and a separate acquisition by Dyal increasing its existing minority interest. All equity acquired was newly issued by Halcyon (terms not disclosed)
Triton Pacific Investment Corporation, Inc., a publicly registered non-traded business development company company; Triton Pacific Capital Partners is an affiliated private equity firm with approximately $1 billion in assets and offerings	**Pathway Capital Opportunity Fund, Inc.**, a registered closed-end investment company	Definitive merger agreement creating TP Flexible Income Fund, Inc., (the “Fund”), which is jointly owned by Triton and Pathway through Prospect Flexible Income Management, an RIC with approximately $6.2 billion in AUM. Pathway shareholders will receive an undisclosed number of TPIC shares with a net asset value equal to the net asset value of the Pathway shares they hold, as determined shortly before closing. The Fund will be a non-traded registered fund structured as a business development company
Victory Capital Holdings, Inc., an investment management firm with approximately $63.6 billion AUM	**Harvest Volatility Management, LLC**, a derivative asset management firm with approximately $12 billion in AUM	Acquisition through a combination of debt, equity and cash on the balance sheet, with the potential for an earn-out over time if certain growth objectives are met. (terms not disclosed)
Victory Capital Holdings, Inc., an investment management firm with approximately $63.6 billion AUM	**USAA Asset Management Company**, a family of companies providing insurance, banking and retirement products with approximately $69.2 billion in AUM	Acquisition for $850 million plus additional contingent payments based on future business performance. Victory Capital will finance the transaction through a combination of debt and cash on the balance sheet

3rd Quarter / 4th Quarter 2018 Closed-End Fund Public Offerings

American Beacon Apollo Total Return Fund

Structure:	An interval fund that will offer to make repurchases of no less than 5% and no more than 25% of its outstanding shares at NAV, on a quarterly basis.
Investment Objectives/Policies:	The Fund seeks to generate attractive risk-adjusted total returns using a multi-sector approach to fixed income value investing. The Sub-Advisor will invest the Fund's assets using a multi-sector approach across a broad range of credit-oriented markets. The Fund is expected to allocate dynamically across the credit universe to the areas which the Sub-Advisor believes produce the most attractive risk-adjusted returns. The Sub-Advisor will utilize a flexible value investment style and will allocate the Fund's assets across four areas: U.S. corporate credit, global corporate credit, structured credit, and real estate credit. The Sub-Advisor will seek to invest the Fund's assets in both secured and unsecured obligations such as: loans; high yield bonds; stressed or distressed credit assets; securities related to debtor-in-possession financing, rescue financing or exit financing; securities related to a corporate reorganization or restructuring; corporate notes, bonds and other investments; RMBS; CMBS; asset-backed securities; emerging market investments; structured credit assets (including CLOs and customized commercial and consumer obligations); infrastructure and infrastructure-related investments; and any other asset or instrument having a similar target return profile. The Sub-Advisor may invest in any level of the capital structure, including senior, mezzanine and subordinated debt.
Manager:	American Beacon Advisors, Inc.; Sub-Advisor: Apollo Credit Management, LLC
Distributor:	Resolute Investment Distributors, Inc.

American Beacon Sound Point Enhanced Income Fund

Structure:	Interval fund that will offer to make repurchases of no less than 5% and no more than 25% of its outstanding shares at NAV, on a quarterly basis.
Investment Objectives/Policies:	The Fund seeks to provide high current income and, secondarily, capital appreciation. The Fund seeks to achieve its investment objectives by investing primarily in a variety of credit-related instruments, including corporate obligations and securitized and structured issues of varying maturities. Corporate obligations may include fixed and floating-rate securities and bank loans, among others, issued by U.S. or foreign (non-U.S.) entities. The mix of assets in which the Fund may invest will be flexible and responsive to market conditions; however, the Manager and Sub-Advisor expect, under normal circumstances, bank loans to constitute at least 40% of the Fund's managed assets. Bank loans may include first-lien and second-lien loans, among other loan types. Securitized issues primarily include CLOs, and structured notes generally include CLNs. The Fund also expects to have exposure to equity-related securities, which typically include the equity tranches of securitized issues. Instruments may be issued by public or private entities and may be restricted as to the type of entity or investor that may transact in them. The Fund may invest without limit in securities rated below investment grade and in unrated securities. The Fund may invest in the obligations of companies undergoing an actual or anticipated corporate event, transaction or other catalyst, which is sometimes referred to as "event-driven" investing.
Manager:	American Beacon Advisors, Inc.
Distributor:	Resolute Investment Distributors, Inc.

3rd Quarter / 4th Quarter 2018 Closed-End Fund Public Offerings *(continued)*

Broadstone Real Estate Access Fund

Structure:	An interval fund that will provide limited liquidity by offering to make quarterly repurchases of each class of shares at that class of shares' NAV.
Investment Objectives/Policies:	The Fund's investment objective is to seek to generate a return comprised of both current income and long-term capital appreciation with low-to-moderate volatility and low correlation to the broader markets. Under normal circumstances, the Fund intends to invest at least 80% of the Fund's net assets in a portfolio of institutional quality real estate and real estate-related investments, which will be comprised of the following primary asset classes: (i) Direct Real Estate Investments, (ii) Private CRE Investment Funds, (iii) Publicly Traded CRE Securities, and (iv) CRE Debt Investments.
Manager:	Broadstone Asset Management, LLC
Distributor:	ALPS Distributors, Inc.

Flat Rock Opportunity Fund

Structure:	An interval fund that will offer to make repurchases of no less than 5% and no more than 25% of its outstanding shares at NAV, on a quarterly basis.
Investment Objectives/Policies:	The Fund's investment objective is to generate current income and, as a secondary objective, long-term capital appreciation. The Fund expects to invest primarily in the equity and, to a lesser extent, in the junior debt tranches of CLOs that own a pool of senior secured loans made to companies whose debt is rated below investment grade or, in limited circumstances, unrated ("Senior Secured Loans"). We may, to a lesser extent, invest in (i) debt and equity securities issued by business development companies, (ii) Senior Secured Loans directly, (iii) fixed income securities and (iv) investment funds that provide exposure to Senior Secured Loans and fixed income securities. The CLOs in which we intend to invest will generally be comprised of Senior Secured Loans that meet specified credit and diversity criteria and are subject to concentration limitations in order to create an investment portfolio that is diversified by borrowers and industries.
Manager:	Flat Rock Global, LLC
Distributor:	ALPS Distributors, Inc.

3rd Quarter / 4th Quarter 2018 Closed-End Fund Public Offerings *(continued)*

NexPoint Healthcare Opportunities Fund

Structure:	Interval fund that will offer to make repurchases of no less than 5% of its outstanding shares at NAV, on a quarterly basis.
Investment Objectives/Policies:	The Fund's investment objective is to seek total return consisting of current income and longer-term capital appreciation. The Fund pursues its investment objective by investing, under normal circumstances, at least 80% of its total assets in the securities of Healthcare Companies. A company will be deemed to be a Healthcare Company if, at the time the Fund makes an investment in a company, 50% or more of such company's sales, earnings or assets arise from or are dedicated to healthcare products or services or medical technology activities. Healthcare Companies are considered by the Adviser to include companies in one or more of the following sub-sectors: pharmaceuticals, biotechnology, managed care, life science and tools, healthcare technology, healthcare services, healthcare supplies, healthcare facilities, healthcare equipment, healthcare distributors, health and wellness, cosmetics and skin care and Healthcare REITs. Additionally, we consider the term Healthcare Company to include companies that are materially impacted by the healthcare industry, such as a contractor that primarily derives its revenue or profit from the construction of hospitals. The Fund may invest in equity and debt securities.
Manager:	NexPoint Advisors, L.P.
Distributor:	Highland Capital Funds Distributor, Inc.

OFI Carlyle Private Credit Fund

Structure:	An interval fund that will offer to make repurchases of no less than 5% and no more than 25% of its outstanding shares at NAV, on a quarterly basis.
Investment Objectives/Policies:	The Fund's investment objective is to produce current income. The Fund seeks to achieve its investment objective by opportunistically allocating its assets across a wide range of credit strategies. Under normal circumstances, the Fund will invest at least 80% of its assets in private fixed-income securities and credit instruments. The Fund will opportunistically allocate its assets across any number of the following credit strategies: (a) liquid credit (including publicly traded debt instruments and Treasury securities); (b) direct lending (including first lien loans, second lien loans, unitranche loans and mezzanine debt); (c) opportunistic credit (including private credit solutions, special situations and market dislocations); and (d) loans and structured credit (syndicated loans and CLOs). To a lesser extent, the Fund also may invest in distressed credit (distressed-for-control debt and equity investments).
Manager:	OC Private Capital
Distributor:	OppenheimerFunds Distributor, Inc.

3rd Quarter / 4th Quarter 2018 Closed-End Fund Public Offerings *(continued)*

Pioneer ILS Bridge Fund

Structure:	An interval fund that will offer to make repurchases of no less than 5% and no more than 25% of its outstanding shares at NAV, on a quarterly basis.
Investment Objectives/Policies:	The fund's investment objective is total return. The fund invests primarily in insurance-linked securities ("ILS"). ILS include event-linked bonds (also known as insurance-linked bonds or catastrophe bonds), quota share instruments (also known as "reinsurance sidecars"), collateralized reinsurance investments, industry loss warranties, event-linked swaps, securities of companies in the insurance or reinsurance industries, and other insurance- and reinsurance-related securities. Because ILS are typically rated below investment grade or unrated, a substantial portion of the fund's assets ordinarily will consist of below investment grade (high yield) debt securities. Investment in securities of below investment grade quality involves substantial risk of loss. Securities in which the fund may invest may also be subordinated or "junior" to more senior securities of the issuer.
Manager:	Amundi Pioneer Asset Management, Inc.
Distributor:	Amundi Pioneer Distributor, Inc.

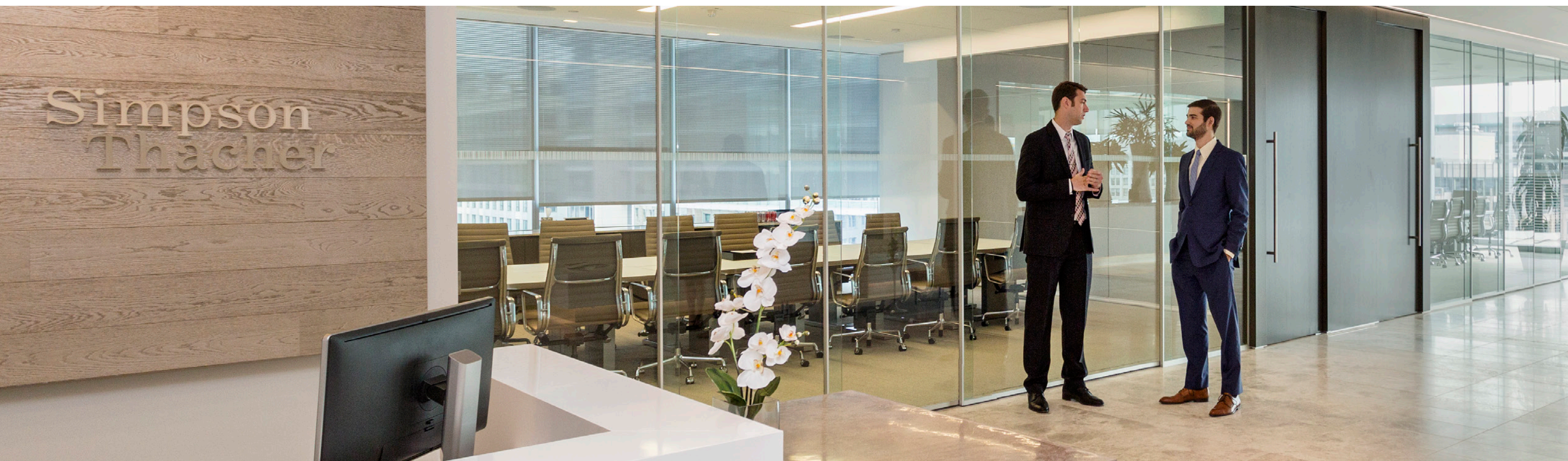
RiverNorth Opportunistic Municipal Income Fund, Inc.

Structure:	A limited term fund, terminating on or before October 25, 2030 unless otherwise determined by the Funds' Board of Directors.
Investment Objectives/Policies:	The Fund's primary investment objective is current income exempt from regular U.S. federal income taxes. The Fund's secondary investment objective is total return. Under normal market conditions, the Fund will seek to achieve its investment objectives by investing, directly or indirectly, at least 80% of its Managed Assets in municipal bonds, the interest on which is, in the opinion of bond counsel to the issuers, generally excludable from gross income for regular U.S. federal income tax purposes, except that the interest may be includable in taxable income for purposes of the Federal alternative minimum tax ("Municipal Bonds"0. In order to qualify to pay exempt-interest dividends, which are items of interest excludable from gross income for federal income tax purposes, the Fund will seek to invest at least 50% of its Managed Assets directly in such Municipal Bonds.
Manager:	RiverNorth Capital Management, LLC
Distributor:	First Dominion Capital Corp.

3rd Quarter / 4th Quarter 2018 Closed-End Fund Public Offerings *(continued)*

Variant Alternative Income Fund

Structure:	Interval fund with quarterly repurchase offers of no less than 5% of the Fund's Shares outstanding at NAV.
Investment Objectives/Policies:	The Fund's primary objective is to provide a high level of current income. Capital appreciation will be considered a secondary objective. Under normal market conditions, the Fund will seek to achieve its investment objective by investing, directly or indirectly through a wide range of investment vehicles, a majority of its net assets in alternative income-generating investments. Such investments are typically domestic and foreign privately-held investments that are outside of traditional public equity and bond markets. These positions typically generate an interest payment, pay dividends, or have other forms of distributions that generally accrue value over time. These assets may include, but are not limited to, real estate equity and debt securities, life settlements, receivables, specialty finance, litigation finance-related investments, royalties, transportation finance, collateralized loan obligation warehouse facility investments, as well as purchases of interests in private credit funds in the secondary market. The Fund may also invest in public securities, including public debt, master limited partnerships, business development companies, and preferred stock. The Fund will allocate its investments across multiple strategies in both developed and emerging markets with varying levels of liquidity and credit quality, including distressed and defaulted investments. The Fund may use derivative investments and may have exposure to long and short positions across its asset classes to obtain the desired risk exposure consistent with its investment strategies.
Manager:	Variant Investments, LLC
Distributor:	Foreside Fund Services, LLC



Simpson Thacher's dynamic, long-standing Registered Funds Practice encompasses all aspects of the investment management business. Our practice focuses on alternative asset managers seeking to access retail investor channels, asset management mergers and acquisitions, and advising on cutting-edge regulatory policy and strategy matters.

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David Blass is a Partner in Simpson Thacher & Bartlett LLP's Investment Funds Practice. David is a leading regulatory lawyer in the funds industry and has advised on matters involving innovative registered funds products, Investment Advisers Act compliance, SEC examination and enforcement matters, and broker-dealer regulatory compliance. Prior to joining Simpson Thacher, David served as General Counsel of the Investment Company Institute (ICI), where he was responsible for the full range of legal and regulatory matters affecting the asset management industry, including investment company, capital markets, pension and tax issues. He also previously was Chief Counsel of the SEC's Division of Trading and Markets.

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Rajib Chanda is a Partner in the Washington, D.C. and New York offices of Simpson Thacher & Bartlett LLP, and is the Head of the Firm's Registered Funds Practice. Rajib's practice focuses on all aspects of issues facing registered investment advisers and sponsors of registered funds. Rajib has particular experience working with alternative asset managers seeking to access retail investor channels through mutual funds, business development companies, closed-end funds, exchange-traded funds and permanent capital vehicles. He also works extensively with more traditional registered fund sponsors and works closely with the firm's asset management M&A group on transactions involving registered advisers and funds. In addition, Rajib provides counsel to boards of registered funds, and has substantial experience advising companies on issues relating to social media and cybersecurity.

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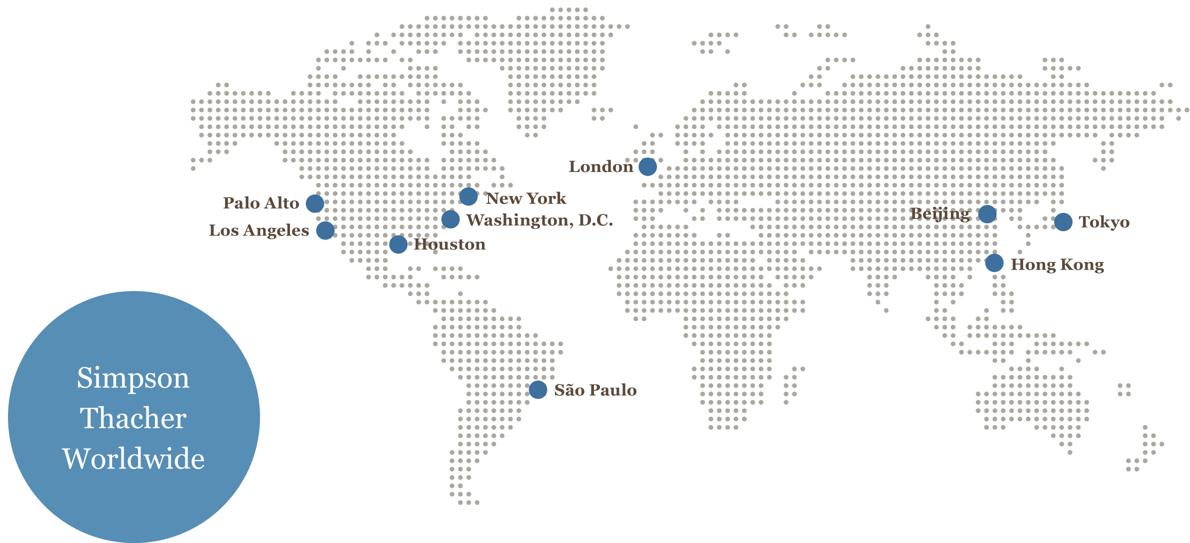

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