22-407

In the United States Court of Appeals
for the Second Circuit

SABA CAPITAL CEF OPPORTUNITIES 1, LTD., SABA CAPITAL MANAGEMENT, L.P.,

Plaintiffs-Appellees,

v.

NUVEEN FLOATING RATE INCOME FUND, NUVEEN FLOATING RATE INCOME OPPORTUNITY FUND, NUVEEN SHORT DURATION CREDIT OPPORTUNITIES FUND, NUVEEN GLOBAL HIGH INCOME FUND, AND NUVEEN SENIOR INCOME FUND; AND TERENCE J. TOTH, JACK B. EVANS, WILLIAM C. HUNTER, ALBIN F. MOSCHNER, JOHN K. NELSON, JUDITH M. STOCKDALE, CAROLE E. STONE, MARGARET L. WOLFF, ROBERT L. YOUNG, AND MATTHEW THORNTON, III, IN THEIR CAPACITY AS TRUSTEES OF THE NUVEEN TRUSTS,

Defendants-Appellants.

On Appeal from the United States District Court
for the Southern District of New York, No. 21-cv-327,
Hon. J. Paul Oetken, *United States District Judge*

**BRIEF OF BULLDOG INVESTORS, LLP
AS AMICUS CURIAE IN SUPPORT OF APPELLEES**

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(SEC No-Action Letter Nov. 15, 2010) 1

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SEC, Report on Investment Trusts and Investment Companies,
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Statement of Commissioner Robert E. Healy Before Subcommittee
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CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure, Bulldog Investors, LLP certifies that it has no parent corporation and no publicly owned corporation owns 10% or more of its stock.

STATEMENT OF INTEREST[1]

Bulldog Investors, LLP ("Bulldog") is an SEC-registered investment adviser that advises a closed-end investment fund and certain separately managed accounts. Among other investment strategies, Bulldog purchases the stock of underperforming closed-end funds at significant discounts to net asset value ("NAV") and may seek to influence management to take actions designed to enhance shareholder value. Bulldog, and its co-founder Phillip Goldstein, have advocated for decades through regulatory and judicial proceedings to permit ordinary shareholders to hold investment advisers accountable for advancing their own self-interests over those of shareholders. Bulldog, like all investors in closed-end funds, has a vested interest in the outcome of this litigation because it will directly determine the ability of incumbent investment advisers of closed-end funds to avoid accountability to shareholders and entrench themselves regardless of the performance of the funds they manage.

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[1] No party's counsel has authored this brief in whole or in part, and no person other than amicus or its counsel contributed money intended to fund the preparation or submission of this brief. All parties to this appeal have consented to the filing of this amicus brief.

INTRODUCTION

This case can be resolved on the plain language of Section 18(i) of the Investment Company Act of 1940 (the "1940 Act"), which provides that all stock of an investment company "shall be a voting stock and have equal voting rights with every other outstanding voting stock." Section 18(i) clearly prohibits investment companies from using inequitable governance devices—like the control-share measure at issue here—to disenfranchise a particular class of shareholders. The decision below was a well-reasoned application of Section 18(i), and should be affirmed on that basis. If, however, this Court finds the history of the 1940 Act to be relevant to its decision, Bulldog respectfully submits this brief to correct certain historical inaccuracies presented by Appellants and its amicus curiae.

Contrary to Appellants' retelling, the 1940 Act had nothing to do with concerns about activist shareholders, but rather sought to eliminate abusive practices *by fund managers* to perpetuate control over their funds against the wishes of security holders. Indeed, while control-share voting limitations are recent developments,[2] defensive devices of their ilk were among the very abuses that gave

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[2] The adoption of control-share bylaws was fueled by the SEC's withdrawal, in 2020 under the prior administration, of the so-called Boulder No-Action Letter, which concluded that the use of such bylaws is inconsistent with Section 18(i). *See Boulder Total Return Fund, Inc.*, File No. 811-07390, 2010 WL 4630835, at *2 (SEC No-Action Letter Nov. 15, 2010).

rise to the 1940 Act, including Section 18(i). The SEC has long recognized the "primary importance" of protecting shareholder voting rights—as Section 18(i) is designed to do—so that an investor has a fair "opportunity to supplant the management of his investment company when the conduct of those representatives no longer meets with his approval." SEC, Report on Investment Trusts and Investment Companies, H.R. Doc. No. 279, 76th Cong., 1st Sess. (1940) ("SEC Report III") at 1874.

Appellants' narrative about protecting "long-term" investors is a façade. All shareholders are harmed by having an entrenched and unaccountable investment adviser, and Nuveen has no actual knowledge, in any event, of its shareholders' preferences or the percentage of investors that it claims to be "long term." Nuveen has simply invented, for purposes of this litigation, a proverbial "long-term" investor whose preferences are always aligned with Nuveen's. But even if these blind loyalists existed, Nuveen would have no basis under the 1940 Act to give unfair preference to those investors over others. For precisely these reasons, Section 18(i) was passed to ensure that important matters regarding an investment company are decided by all shareholders through a vote that objectively tallies their preferences commensurate with their economic interests in the outcome. The control-share provisions at issue in this case are merely a new variation of the breed of vote rigging that stirred Congress to pass the 1940 Act.

BACKGROUND

Investment companies are pools of assets owned by their shareholders, not their sponsoring investment advisers. Although sponsors may initially organize a fund and its board of trustees, they are thereafter arm's-length service providers that serve at the pleasure of shareholders. While all shareholders of a closed-end fund hold the right to determine significant policies, including firing the adviser,[3] small investors typically lack the time and resources to play an active part in overseeing a fund's management.[4] Large and sophisticated investors, like closed-end fund activists, thus play a key role by contributing the expertise and resources necessary to oversee an adviser's conduct. Activists typically identify funds with significant potential for improvement or a value-maximizing transaction, and they purchase a significant percentage of outstanding shares so as to make it economically viable to engage with management (for example, to pay the expenses associated with

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[3] Section 15(a)(3) of the 1940 Act, 15 U.S.C. § 80a–15(a)(3), provides that a management contract may be "terminated at any time, without the payment of any penalty . . . by vote of a majority of the outstanding voting securities of such company."

[4] *See* Robert F. Wagner, *Senator Wagner Introduces Investment Trust Legislation* (March 14, 1940) (https://tinyurl.com/5n6v4ywv) (noting in connection with introducing the 1940 Act that the "financial resources of the average stockholder are usually insufficient to meet the burden of complicated and long-drawn-out judicial and other proceedings which may be necessary to oppose successfully unfair management-prepared plans.").

soliciting proxies to elect new trustees). Activists routinely share the same financial interests as other shareholders, but have the means to pursue those interests in a meaningful way.

The work of shareholder activists tends to bring into sharp contrast the ever-present tension between investors and managers: that an incumbent manager is typically not motivated to enact change that would threaten to reduce or eliminate its fees, even if such changes would materially benefit shareholders. Activist shareholders, with their expertise and resources, provide the catalyst to bring about beneficial change when an incumbent manager is unwilling to do so.

In this case, Appellants have adopted control-share measures in order to cap an individual shareholder's voting power at 10% of the Funds' outstanding shares, significantly curtailing the ability of activist shareholders to check Nuveen's conduct as manager. These measures violate both the plain text of Section 18(i) of the 1940 Act and Congress's purpose in adopting it.

ARGUMENT

I. THE 1940 ACT WAS PASSED TO ADDRESS ABUSIVE PRACTICES BY INCUMBENT FUND MANAGERS

In the early decades of the 20th century, investment companies operated in an "atmosphere of self-dealing [by insiders] and conflicting interests," and the "pecuniary interest of the promoters, distributors and managers dominated almost every phase of the organization and operation of investment companies to the

detriment of investors." *See* Robert F. Wagner, *Senator Wagner Introduces Investment Trust Legislation* (March 14, 1940) (https://tinyurl.com/5n6v4ywv) ("Senator Wagner Release") at 2. The 1940 Act was born out of these systemic abuses by fund managers and other insiders, like Nuveen, not activist shareholders, like Saba. *See* Statement of Commissioner Robert E. Healy (April 2, 1940) (https://tinyurl.com/3fzjajfw) at 4 (stating to Congress that the SEC's investigation into the industry found that "too often investment trusts and investment companies were organized and operated as adjuncts to the business of the sponsors and insiders to advance their personal interest at the expense of and to the detriment of their stockholders").

In introducing the 1940 Act, Senator Wagner catalogued some of the "abuses and deficiencies" within the industry, including, as relevant here, that "in many cases" fund managers had made their funds "impregnable" through the use of "management voting stock [and establishing a] form of organization in which security holders have no vote," "long-term management contracts which also assured substantial compensation irrespective of the company's performance," and "domination of the proxy machinery for the solicitation of authority to vote the shares held by public stockholders." Senator Wagner Release at 2. He likewise noted frequent instances in which fund managers had "used their control of the applicable corporate and statutory machinery to subject stockholders to inequitable

readjustments of the rights, privileges, preferences and values of their securities." *Id.* at 3.

The 1940 Act brought order to the industry and standardized the capital structure of investment companies in a manner that protected the rights of investors to control their fund commensurate with their economic interests (*i.e.*, in an equitable way). That protection was effectuated, in part, by Section 18(i), 15 U.S.C § 80a–18(i), which did away with manipulative capital structures that consolidated voting power with fund managers and their affiliates by requiring that all common stock of an investment company "shall be a voting stock and have equal voting rights with every other outstanding voting stock."

II. SECTION 18(i) PROHIBITS THE USE OF INEQUITABLE DEVICES DESIGNED TO PERPETUATE CONTROL

Section 18(i) resulted from decades of manager-led schemes to insulate themselves from the will of unaffiliated shareholders. The use of creative governance provisions to perpetuate control is as old as the investment trust itself, and the SEC found in its congressional reports preceding the 1940 Act that a "complex capital structure has been an important element in fostering and facilitating many of the abuses which have characterized that industry." SEC Report III at 1566.

For example, the SEC found that advisers retained control over investment companies through utilization of dual classes of common stock: Class A "intended

primarily for distribution to the public" and Class B "designed for the sponsor." SEC Report III at 1620. Not surprisingly, Class A stock "brought the major contribution to the capital of the company," but was "awarded little voting power" and sometimes none at all.[5] *Id.* Other self-dealing devices included corporate forms with limited voting rights, including a "type of trust where the shareholders are not given the right to vote,"[6] *id.* at 1891, options or warrants that "fortified against any threat to [an adviser's] control since it could always exercise sufficient of these warrants to insure adequate voting power, *id.* at 1895, and convertible securities with the same effect.

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[5] Interesting examples of the two-tiered structure abound in the SEC's reports. In one case, public shareholders had no voting rights at all despite contributing virtually all of the capital, SEC Report III at 1623; in another case public shareholders were entitled to one vote per share in a director election but insiders were entitled to "the number of shares multiplied by the number of directors to be elected," *id.* at 1627; in another case public shareholders were entitled to "one-half of the voting power of the total outstanding common stock," *id.* at 1632; and in another case insiders had "three votes per share" whereas public shareholders had only one. *Id.* at 1631.

[6] Appellants rely on state common law throughout their brief, but an absence of effective state regulation (or worse, a "race to the bottom" by state legislatures) was a primary reason that Congress passed comprehensive federal legislation. The SEC noted Massachusetts business trusts, which granted no voting rights and thus shareholders had "no voice in the selection or change in the trustees or management," as well the "flexible incorporation laws of Maryland and Delaware law." SEC Report III at 1028, 1890; *see also Louis K. Liggett Co. v. Lee*, 288 U.S. 517, 557–60 (1933) (as of 1933, "states, eager for the revenue derived from the traffic in charters, had removed safeguards from their own incorporation laws. Companies were early formed to provide charters for corporations in states where the cost was lowest and the laws least restrictive. The states joined in advertising their wares. The race was one not of diligence but of laxity.").

Id. at 1899. As a result, by 1935, fund managers and their "affiliated interests" controlled the "majority voting power" in a significant percentage of all investment companies with more than $500,000 in assets. *Id.* at 1875. This control was rarely if ever commensurate with capital contribution; rather, advisers routinely obtained majority voting power with "no contribution or a very small contribution to the capital investment." *Id.* at 1620. Section 18(i) addressed the inequitable control schemes at the time as well as potential future schemes with simple efficiency: it states that "every share of stock . . . shall be a voting stock and have equal voting rights." The rationale articulated by the SEC at the time rings just as true today:

> [The] primary importance [of capital structure] to the investor is his opportunity to supplant the management of his investment company when the conduct of those representatives no longer meets with his approval. The divorcement of control over management from the ownership of the investment company almost invariably presents vital problems. The problems are most acute where the insulation of management from ownership is complete—where the beneficial owners of the fund are deprived of any voice in the conduct of management.

SEC Report III at 1874.[7]

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[7] The SEC also recognized the special problem of managerial accountability within closed-end funds, "where the shareholder does not have the right to compel redemption of his shares at asset value," and "must dispose of his securities in the open market [when] these securities may be selling at substantial discounts from their asset values." SEC Report III at 1874.

Nuveen's efforts to preserve its control through the control-share measures at issue in this case are of the same nature, purpose and effect as the abuses that motivated Congress to adopt Section 18(i). Rather than directly consolidating control with Nuveen and its affiliates, the bylaws take another approach to the same end: they disenfranchise large shareholders in order to weaken their ability to challenge Nuveen's control. Either way, such disenfranchisement is precisely what Section 18(i) was intended to prohibit.

III. THE 1940 ACT WAS NOT PASSED <u>TO DETER ACTIVIST SHAREHOLDERS</u>

Of the thousands of single-spaced pages of the SEC's "intensive" reports to Congress that preceded the 1940 Act,[8] and of all the publicly available legislative statements and materials, Appellants have cobbled together only a handful of pages from the SEC's reports purportedly showing a concern about closed-end fund activists. *See* Opening Brief at 31. There was no such concern at the time. The pages cited address abuses by *fund managers* who were extracting the value of closed-end

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[8] *See* Brief and Special Appendix for Appellants Nuveen Floating Rate Income Fund, et al. (ECF 60) ("Opening Brief") at 8-9 (citing SEC, Report on Investment Trusts and Investment Companies, H.R. Doc. No. 707, 75th Cong., 3d Sess. (1939) (SEC Report I); H.R. Doc. No. 70, 76th Cong., 1st Sess. (1939) (SEC Report II); H.R. Doc. No. 279, 76th Cong., 1st Sess. (1940) (SEC Report III)).

funds from shareholders through undisclosed sales and mergers (*i.e.*, sweetheart deals), not the work of activist shareholders.[9]

Before the 1940 Act, investment advisers had, in numerous instances, covertly sold control of investment companies to acquirers who would, through a combination of collusive transactions and coerced "exchange offers," extract any remaining value from the fund without sharing it with investors. *Id.* Indeed, the SEC recognized that "in many cases, a dissolution of the investment companies rather than a shift in control would have prevented the losses which frequently resulted" and "would have resulted in the stockholders receiving [the] companies' assets." *Id.* But selling control of the fund was more "pecuniarily attractive for sponsors and managers" who "would have received nothing in the event of a dissolution." *Id.* at 1022-23. Thus, the critical distinction between the pre-1940 abuses by insiders and

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[9] Specifically, the SEC found that the "crash in the securities markets in 1929 and the resultant sharp losses suffered by investment companies created public disfavor of such companies and their managements," which was "reflected in the substantial discounts [of funds] from their asset values." SEC Report III at 1017. Because the "management contracts . . . their investment companies had become of little value," the pecuniary benefits of serving as a fund's manager "substantially diminished" and many investment advisers were "desirous of severing their connections with their investment companies." *Id.* at 1018. This ushered in an "era of transfers of control and acquisition" through which fund managers took advantage of regular shareholders by extracting value from a fund only for the benefit of the manager and its counterparties. *Id.* Sometimes these schemes profited insiders by diverting the spread between a fund's NAV and market price, but those sort of sweetheart deals bear no analogy to closed-end fund activism.

shareholder activism of today is that the former involved collusive transactions with a *fund's manager* to profit at the expense of shareholders—*i.e.*, "sell[ing] their stockholders down the river," SEC Report III at 1022—whereas activists are unaffiliated with a fund's manager and other insiders, and any benefits they achieve are shared with all other shareholders.

Contrary to Appellants' version of history, the congressional record suggests an *acute need for more and better activist shareholders*, which would have pushed investment advisers to take value-maximizing actions, like liquidation. The SEC noted an incumbent manager's "control over the proxy machinery . . . provides a formidable defense against threats to their continued tenure of office," including "ready access to stockholders' lists and to corporate funds for the solicitation of proxies." "An opposing group, even if it made out a strong case for a change of management, would be confronted with the task of overcoming the inertia," and thus the SEC observed that "in almost every case where the original sponsors placed their representatives in positions of control over investment companies, this control, except where voluntarily surrendered, has continued and is still exercised." SEC Report III at 1877.

One of the only examples of a shareholder overcoming management's incumbent control, before the 1940 Act sought to level the playing field, involved the Standard Investing Corporation. As recounted by the SEC, the sponsor obtained

initial control of the fund in 1927 by *giving itself* 25,000 shares as a "promotion fee," and issuing 15,000 shares to the public. SEC Report III at 1883. By 1936, however, there were nearly 400,000 shares outstanding, and the "declining markets following the market crash of 1929" "accentuated the vulnerability of management control" because the value of the common shares fell precipitously and was dwarfed in comparison to the fund's debt obligations. *Id.* The Phoenix Securities Corporation began to acquire shares and held about "30% of the total common shares outstanding" when it launched a proxy war against the manager. *Id.* at 1883-84. Despite the "relatively small holdings of the management group," management was able to obtain 40,000 proxies and fend Phoenix off. *Id.* at 1884. However, Phoenix continued to purchase shares, and was eventually able to wrest control from the manager and cause a sale of the fund. *Id.* This rare outcome would have been prevented by the use of defensive mechanisms prevalent at the time (dual-class voting structures) as well as those at issue today (control-share bylaws), both of which are now prohibited by Section 18(i).

IV. APPELLANTS' VERSION OF THE SO-CALLED "LONG-TERM SHAREHOLDER" IS AN INVENTION

The caricature of a "long-term" shareholder in Appellants' briefing—*i.e.*, one that does not care about investment performance or trading discount and only wants Nuveen to forever manage their money—does not accurately reflect reality.

First, Appellants cannot objectively define a "long-term" shareholder other than to say that it is an investor that very much likes Nuveen and never plans to sell shares in the Funds. But it is implausible that an investor of any term would be agnostic to investment performance or the fund's trading discount, much less long-term investors who have the most to lose from protracted underperformance.

Second, Nuveen has no idea what percentage of the Funds' shares are held for the "long-term," and even if it somehow knew as to a particular day, the percentage continuously changes. As Mike Tyson might say if he were an investment professional, "everybody is a long-term shareholder until they get punched in the account" (or simply need to sell).[10] Indeed, shareholders with long-term holding periods sell every trading day for myriad reasons; however, as to the Funds at issue, they often must do so at less than 100 cents on the dollar.

Third, nothing in the 1940 Act suggests that discrimination among types of shareholders is permissible for any reason, including holding period. To the contrary, Section 18(i) guarantees equal voting rights to all investors and precludes a fund

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[10] Mike Berardino, *Mike Tyson explains one of his most famous quotes*, SOUTH FLORIDA SUN-SENTINEL (available at https://tinyurl.com/27bn6j42) (quoting Mike Tyson as stating iconically "Everybody has a plan until they get punched in the mouth").

manager from catering to particular shareholders whose interests purportedly align with those of insiders.[11]

History demonstrates that the only equitable method for holding management accountable to shareholders is by a fair vote in which shareholders are permitted to voice their opinions commensurate with their economic stake. In this case, the Funds' control-share mechanisms preclude such a vote and render it unfair by disenfranchising large shareholders. Just as managers before 1940 rigged the vote by giving themselves greater voting power, Nuveen seeks to achieve the same result by limiting the voting power of others. That result, if permitted, would undermine the purpose and plain language of Section 18(i) and the 1940 Act generally.

CONCLUSION

Section 18(i) of the 1940 Act prohibits the control-share devices at issue in this case, and the lower court's ruling should be affirmed.

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[11] Taking Appellants' approach to its logical extreme reveals how inequitable catering to arbitrary groups of investors can be. Consider a shareholder in one of Nuveen's Funds who owns 80% of all outstanding common stock, but is capped at 10% voting power. Only 30% of outstanding shares would be permitted to vote, and the 20% minority would have absolute control over the fund's management. This is precisely the type of manipulation that gave rise to the 1940 Act. *See, supra,* n. 4.

Dated: September 15, 2022

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

This brief complies with the type/volume limitations of Fed. R. App. P. 29(a)(5) because the brief contains 3,633 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f). The brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the typestyle requirements of Fed. R. App. P. 32(a)(6), because this brief has been prepared in a proportionally spaced typeface using 14-point Times New Roman font.

CERTIFICATE OF SERVICE

I hereby certify that on this 15th day of September 2022, I caused true and accurate copies of the foregoing to be served on counsel of record via the CM/ECF system.

/s/ Andrew W. Robertson
Andrew W. Robertson

Dated: September 15, 2022