

Section 6910, *Investment Companies*



.38 Determining If Liquidation Is Imminent When the Only Investor in an Investment Company¹ Redeems Its Interest, and the Investment Company Anticipates Selling All of Its Investments and Settling All of Its Assets and Liabilities

Inquiry—When the only investor in an investment company redeems its interest, and, as a result, the investment company anticipates selling all of its investments and settling all of its assets and liabilities, should liquidation be considered imminent? Must it be anticipated that the legal entity will be dissolved in order for liquidation to be imminent?

Reply—It depends on the intent of the sponsor or investment adviser. Factors to consider include whether the sponsor or investment adviser of the investment company anticipates continuing to operate the investment company using the same or a similar investment strategy, and whether the lack of investors is expected to be temporary. It may also depend on the terms of the governing documents as they relate to this situation.

For example, if the sole investor in an investment company redeems its interest and if management does not intend to continue (or may not continue, according to the fund's governing documents) to solicit new investors and does not expect the investment company to continue its previous operations (that is, continue with an investment strategy consistent with its governing documents), the liquidation basis of accounting may be appropriate because this may be considered a plan for liquidation imposed by other forces, and the likelihood may be remote the entity will return from liquidation. However, if management intends to continue to solicit investors under its existing investment strategy, the temporary lack of investors does not necessarily indicate that a forced liquidation is being imposed on the investment company and that liquidation is imminent. There may be situations in which the investment adviser retains the legal entity and uses it to offer investors an investment company with a new name and different investment strategy. In these cases, the activities of the original investment company have ceased, and utilizing the legal entity for a new purpose could indicate that the original entity has effectively liquidated.

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