

SIDLEY UPDATE

# SEC Adopts Offering Reforms for Business Development Companies and Registered Closed-End Funds

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April 21, 2020

On April 8, 2020, the U.S. Securities and Exchange Commission (the SEC) adopted rule and form amendments (the Amendments) allowing business development companies (BDCs) and closed-end investment companies registered under the Investment Company Act of 1940, as amended (the 1940 Act) (Registered CEFs and, together with BDCs, Affected Funds), to use the securities offering rules available since 2005 for other issuers (i.e., operating company issuers) that are required to file reports under Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act).<sup>1</sup> Certain of the Amendments apply only to BDCs and Registered CEFs that also qualify as “well-known seasoned issuers” (WKSIs) as defined in Rule 405 (as amended) under the Securities Act of 1933, as amended (the Securities Act).<sup>2</sup> The Amendments modify the registration, communications and offerings processes for Affected Funds.

*Effectiveness of Amendments.* The Amendments generally become effective on August 1, 2020. Amendments to Rules 23c-3, 24f-2 and Form 24F-2 under the 1940 Act, providing a new registration fee payment method for Interval Funds and issuers of certain exchange-traded products (ETPs),<sup>3</sup> and amendments to Rules 456 and 457 and Forms S-1, S-3, F-1 and F-3 under the Securities Act, permitting ETPs to register offerings of an indeterminate number of exchange-traded vehicle securities on those forms and pay registration fees for such offerings on an annual net basis, become effective August 1,

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<sup>1</sup> See “Securities Offering Reform for Closed-End Investment Companies,” SEC Release No. 33-10771 (April 8, 2020) (<https://www.sec.gov/rules/final/2020/33-10771.pdf>) (the Adopting Release). The proposing release relating to securities offering reform for closed-end investment companies was issued on March 20, 2019, *Securities Offering Reform for Closed-End Investment Companies*, Investment Company Act Release No. 33427 (March 20, 2019) (the Proposing Release).

<sup>2</sup> In 2018, Congress passed the Small Business Credit Availability Act (the SBCA Act), which, among other things, directed the SEC to revise certain securities offering and proxy rules to reduce disparities in registration and reporting requirements for BDCs as compared to other issuers, and the Economic Growth, Regulatory Relief and Consumer Protection Act (the Economic Growth Act), which directed the SEC to propose and finalize rules and regulations to allow a Registered CEF listed on a national securities exchange (a Listed Registered CEF) or a Registered CEF that makes periodic repurchase offers pursuant to Rule 23c-2 under the 1940 Act (an Interval Fund) to use the securities offering and proxy rules currently available to other issuers that are required to file reports under Section 13(a) or Section 15(d) of the Exchange Act. The SBCA Act applies to all BDCs, whether listed on an exchange or not. The Economic Growth Act does not mandate rulemaking for unlisted closed-end funds; however, the SEC has proposed to extend the proposed securities offering and communications rules, with some exceptions, to unlisted closed-end funds. The Adopting Release notes that while unlisted Affected Funds (such as Interval Funds) may not qualify to rely on all the Amendments, they will be able to rely on some rules that may provide additional flexibility.

<sup>3</sup> The Adopting Release defines ETPs as “issuers that are not registered investment companies and whose assets consist primarily of commodities, currencies or derivative instruments that reference commodities or currencies; whose securities are listed for trading on a national securities exchange; and that purchase or redeem securities for a ratable share of their assets at NAV” (net asset value).

2021. In the Adopting Release, the SEC notes that the delayed effectiveness of those amendments is necessary to provide the SEC with sufficient time to update its systems.

*Delayed Compliance Dates for Certain New Requirements.* The SEC is providing a transition period for compliance with certain requirements by delaying compliance dates, as described below:

- The compliance date for the requirement for Registered CEFs to include management's discussion of fund performance (MDFP) in their annual reports to shareholders is August 1, 2021.
- The compliance date to comply with new structured data requirements (using Inline XBRL format) for Affected Funds eligible to file a short-form registration statement is August 1, 2022. The compliance date for all other Affected Funds subject to these requirements is February 1, 2023. Affected Funds will be permitted to file in Inline XBRL prior to the compliance date after EDGAR has been modified to accept the submissions, anticipated to be in March 2021.
- The compliance date for 24F-2 filers to file reports on the form in an XML structured data format is February 1, 2022.

See "*Disclosure and Reporting Parity Amendments*" below.

### **Highlights**

The Amendments enable eligible Affected Funds to use securities offering rules that are currently available only to certain operating company issuers, including rules relating to

- use of short-form registration statements and forward incorporation by reference
- WKSJ status for eligible Affected Funds
- automatic or immediate effectiveness for filings by Affected Funds conducting certain continuous offerings
- final prospectus delivery reforms: access equals delivery
- communications reforms
- new registration fee payment method for Interval Funds
- broker-dealer research reports
- disclosure and reporting parity amendments

The Amendments are summarized below, followed by a table, adapted from Table 2 in the Adopting Release, outlining the changes by affected rule or form.

### **Short Form Registration/Forward Incorporation by Reference**

The Amendments allow eligible Affected Funds to sell securities more quickly "off the shelf."<sup>4</sup> The Amendments also clarify and expand the ability of eligible Affected Funds to use rules currently available only to seasoned operating companies: (i) using a "base" prospectus on Form N-2, (ii) relying on Rule 430B under the Securities Act to omit certain information, (iii) incorporating by reference certain *past and*

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<sup>4</sup> The Amendments provide an Affected Fund using Form N-2 flexibility and convenience comparable to that afforded to operating companies using Form S-3. An Affected Fund using a short-form Form N-2 shelf registration statement will no longer need to update its financial statements and other information by filing an annual post-effective amendment subject to SEC staff review. However, the Affected Fund, like an operating company, generally must file a new registration statement every three years to continue using the shelf. See Rule 415(a)(5).

future Exchange Act reports and (iv) using a later prospectus supplement to provide the omitted information.

To be eligible, an Affected Fund must meet the registration and transaction requirements of Form S-3. If the Affected Fund is a closed-end fund, it must have been registered under the 1940 Act for at least 12 calendar months preceding the filing of the registration statement and have timely filed all reports required under Section 30 of the 1940 Act during such time. An Affected Fund would generally satisfy the transaction requirements of Form S-3 for a primary offering if the fund's public float is at least \$75 million.

As most Interval Funds do not list their securities on an exchange and do not have public float, they would not be able to use short-form registration statements that omit information required to be included in the fund's prospectus when it offers its securities. However, Interval Funds can rely on Rule 415(a)(1)(xi) under the Securities Act, which provides some of the same efficiencies.

The Amendments (i) amend Rule 415 under the Securities Act to clarify that Affected Funds may use that rule and (ii) add a new general instruction to Form N-2 to permit Affected Funds that are WKSIs under the Amendments to file an automatic shelf registration statement. A WKSI can register unspecified amounts of different types or classes of securities on an automatic shelf registration statement.

Use of a short-form registration statement and the incorporation by reference of future reports may provide benefits, including (i) a faster registration process and (ii) incremental lower costs (e.g., by permitting such funds to incorporate by reference certain documents or disclosure).

In addition, the Amendments remove the requirement that Affected Funds deliver to new investors information that has been incorporated by reference into the fund's prospectus or statement of additional information (SAI) and instead require the fund to make its prospectus, SAI and the incorporated materials readily available and accessible on a website maintained by or for the fund. The fund is required to provide, at no charge, any materials incorporated by reference, upon request, to any person to whom a prospectus or SAI was delivered.

The Amendments will permit certain Affected Funds to forward incorporate information from their Exchange Act reports. A fund may include information in a periodic report for the purpose of updating its registration statement that is not required to be included for purposes of the periodic filing itself. The Proposing Release proposed to require that a fund that does forward incorporate information from an Exchange Act report include a statement in the report identifying information that it included for the purpose of updating its registration statement, with the intent of providing context for investors. However, to address concerns that requiring such identifying statement in periodic reports may unnecessarily emphasize the information included and distract investors from more material information, the requirement to include such a statement is not included in the Amendments.

### **WKSI Status**

Under the securities offering reform rules adopted in 2005, an issuer that meets certain requirements qualifies as a WKSI and is able to benefit from modified rules relating to communications and the securities registration process. The 2005 offering reforms expressly excluded Affected Funds, with such entities being deemed "ineligible issuers." The Amendments permit an Affected Fund that qualifies as a WKSI to communicate at any time (including by means of a free writing prospectus) without violating the "gun-jumping" provisions of the Securities Act. To qualify as a WKSI, an issuer must (i) satisfy the registration requirements of Form S-3 (i.e., it must be "seasoned") and (ii) generally must have at least \$700 million in "public float" (market value of outstanding voting and nonvoting common equity held by non-affiliates).<sup>5</sup> Alternatively, an issuer can satisfy this requirement if, as of a date within 60 days of the determination date, it has issued, for cash, within the past three years, at least \$1 billion in aggregate principal amount of nonconvertible securities, other than common equity, through primary offerings that

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<sup>5</sup> The determination of public float is based on a public trading market, such as an exchange or certain over-the-counter markets.

were registered under the Securities Act.<sup>6</sup> Despite receiving a number of comments suggesting that the SEC modify the WKSJ definition to enable more Affected Funds to qualify by, for example, reducing the public float requirement, the SEC declined to do so.

An issuer is ineligible for WKSJ status if, among other factors, (i) it is not current and timely in its Exchange Act reports during the prior 12 months (or such shorter period that the issuer was required to file such reports) or (ii) it is the subject of a judicial or administrative decree or order arising out of a governmental action involving violations of the antifraud provisions of the federal securities laws.<sup>7</sup> The Amendments modify the definition of “ineligible issuer” (i) to reflect that a Registered CEF would be ineligible if it has failed to file all reports and materials required to be filed under Section 30 of the 1940 Act during the preceding 12 months and (ii) to provide that an Affected Fund would be ineligible if within the past three years its investment adviser, including any sub-adviser, was the subject of any judicial or administrative decree or order arising out of a governmental action that determines that the investment adviser aided or abetted or caused the Affected Fund to have violated the antifraud provisions of the federal securities laws.

### ***Automatic or Immediate Effectiveness for Filings by Affected Funds Conducting Certain Continuous Offerings***

Under amended Rule 486, certain non-interval Affected Funds that conduct continuous offerings under Rule 415(a)(1)(ix), such as continuously offered tender offer funds, may rely on Rule 486 (regardless of whether or not they are WKSJs) to make changes to their registration statements on an immediately effective basis or automatically after 60 days.

### ***Final Prospectus Delivery Reforms: Access Equals Delivery***

The Amendments amend Rule 172 under the Securities Act to permit an Affected Fund that meets certain requirements to satisfy its final prospectus delivery obligation by filing the prospectus within the time required by the rules and meeting certain other conditions. Rule 173 under the Securities Act requires that a notice be provided to purchasers stating that the sale of securities was made pursuant to a registration statement in which a final prospectus would have been required to be delivered in the absence of Rule 172.

### ***Communication Reforms***

The Amendments permit Affected Funds to use various communications without being deemed to violate the Securities Act “gun-jumping provisions” currently available only to operating companies, including “free writing prospectuses” and communications including regularly released factual business information and forward-looking information. Note, however, that the SEC did not extend the statutory safe harbors from liability in private actions for certain forward-looking information to Affected Funds, determining that such action was outside the scope of the current rule-making. The Amendments permit Affected Funds to

- rely on Rule 134 under the Securities Act to publish factual information about the issuer or an offering, such as “tombstone ads”
- rely on Rule 163A under the Securities Act, which provides that communications by or on behalf of an issuer more than 30 days before the filing date of a registration statement that does not reference a securities offering that is or would be subject to a registration statement will not be deemed to be an offer to sell, offer for sale or offer to buy the securities being offered under the registration statement for purposes of Section 5(c) of the Securities Act

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<sup>6</sup> See paragraph (1)(i)(B)(1) of the definition of WKSJ in Rule 405 under the Securities Act.

<sup>7</sup> See the definition of “ineligible issuer” in Rule 405 under the Securities Act.

- rely on Rules 164 and 433 under the Securities Act to use a free writing prospectus
- for Affected Funds that are reporting companies, rely on Rule 168 under the Securities Act to publish or disseminate regularly released factual business information and forward-looking information at any time, including in advance of a registered offering
- rely on Rule 169 under the Securities Act to continue to publish and disseminate regularly released factual business information that is intended for use by persons other than investors or potential investors.

The Amendments also amend Rule 156 under the Securities Act to clarify that nothing in that rule should be construed to prevent an Affected Fund from qualifying for an exemption under Rule 168 or 169 under the Securities Act. The contents of any Rule 168 or 169 communication remain subject to the antifraud provisions of the federal securities laws.

In addition, the Amendments permit Affected Funds that qualify as WKSIs to engage at any time in oral and written communications, including the use of a free writing prospectus (before or after a registration statement is filed), subject to the same conditions applicable to other WKSIs.

Affected Funds that use Rule 482 advertisements will still be required to file them with the SEC, meaning that a Rule 482 advertisement will continue to constitute a prospectus subject to liability under Section 12 of the Securities Act.

#### ***New Registration Fee Payment Method for Interval Funds***

The Amendments address the manner of payments of securities registration fees by requiring Interval Funds to pay securities registration fees using the same method used by mutual funds and exchange-traded funds, and extending this payment method to issuers that are not registered investment companies of certain continuously offered ETPs.

The Amendments require Interval Funds to pay securities registration fees on a net basis once a year rather than the Interval Fund having to pay when filing its registration statement. In response to comments to the Proposing Release, this treatment is being extended to ETPs.

#### ***Broker-Dealer Research Reports***

Recommendations and other reports published by brokers and dealers can raise issues under Section 5 of the Securities Act when published around the time of a registered securities offering. Rules 137, 138 and 139 under the Securities Act immunize certain recommendations and reports from characterization as illegal offers or as impermissible types of prospectuses. Although the Rule 137 safe harbor has been available to broker-dealers publishing research on the securities of Affected Funds, Rules 138 and 139 have not. All three rules are safe harbors. Rule 139 requires that an issuer that is covered in a research report published in reliance on Rule 138 must have filed all required periodic reports during the prior 12-month period on Forms 10-K and 10-Q. Registered CEFs do not file these reports. The Amendments include references to reports on Forms N-CSR, N-Q, N-CEN and N-PORT in Rule 139, thereby including Registered CEFs in the existing regulatory framework for research reports.

#### ***Disclosure and Reporting Parity Amendments***

The Amendments require Affected Funds to provide certain additional disclosures, including

- for Registered CEFs, MDFP in their annual reports to shareholders<sup>8</sup>

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<sup>8</sup> The Amendments amend Form N-2 to require this disclosure from Registered CEFs.

- for BDCs, financial highlights in their registration statements and annual reports
- for Affected Funds filing a short-form registration statement on Form N-2, disclosure of material unresolved SEC staff comments and, in their annual reports, information regarding (i) fees and expenses, (ii) premiums and discounts and (iii) outstanding securities of the Affected Funds that the Affected Funds currently provide in their prospectuses (without requiring duplicative disclosure)

The Proposing Release included a proposal to require Registered CEFs that are reporting companies under Section 13(a) or Section 15(d) of the Exchange Act to file current reports on Form 8-K regarding material changes to investment objectives or policies and material write-downs of significant investments. However, after considering concerns raised by commenters, the SEC did not adopt those amendments, noting, “[W]e are persuaded that a new Form 8-K reporting requirement for [Registered CEFs] may not substantially improve the flow of important current information to investors and the market and, as a result, would not justify the additional burdens associated with Form 8-K reporting.”

The Amendments remove the exclusion for BDCs from the Inline XBRL financial statement tagging requirements so that BDCs, like operating companies, will be required to submit financial statement information using the Inline XBRL format. In addition, the Amendments require (i) Affected Funds to include structured cover page information in their registration statements using Inline XBRL format, (ii) certain information in an Affected Fund’s prospectus be tagged using Inline XBRL format and (iii) filings on Form 24F-2 (the annual notice of securities sold) be submitted in Extensible Markup Language (XML) format. The Adopting Release notes that the intended purpose of the use of structured data is “to make financial information easier for investors to analyze and to help automate regulatory filings and business information processing, and to reduce the current disparity between operating companies and BDCs with respect to the accessibility of information they provide to the market.” The Adopting Release notes that confidential information will not be required to be disclosed pursuant to these new reporting requirements.

### ***Other Considerations***

- The Amendments amend Rule 8b-16(b) under the 1940 Act to require any Registered CEF that relies on that provision to describe the fund’s current investment objectives, investment policies and principal risks in its annual report, even if there have been no changes to such information in the past year, and expand the existing requirements with respect to disclosure of material changes to such information.
- The Amendments amend Rule 486 under the Securities Act, which will allow any Affected Fund (rather than only Interval Funds) that conducts a continuous offering under Rule 415(a)(1)(ix) (such as a continuously offered tender offer fund) to rely on the rule. Newly eligible Affected Funds relying on Rule 486 generally are required to file new registration statements every three years under Rule 415(a)(5) and (a)(6).
- The Amendments modify Form N-14 to allow BDCs to incorporate by reference to the same extent as Registered CEFs.
- The Amendments allow Affected Funds that meet certain requirements to incorporate certain required information into proxy statements by reference to previously filed documents for proxy statements containing specific proposals.
- Because the common stock of many Listed Registered CEFs currently trades on exchanges at a discount to net asset value, and most Listed Registered CEFs have not obtained stockholder consent as required by Section 23(b)(2) of the 1940 Act to sell common stock at less than net asset value, the Amendments may be of limited practical utility to Listed Registered CEFs seeking to issue additional common stock. However, the Amendments will allow Listed Registered CEFs to access the public capital markets more quickly in the event that the market

discount is eliminated. In addition, Listed Registered CEFs that engage in rights offerings or use leverage by means of issuing preferred stock or debt may find the Amendments helpful in being able to access the public capital markets in a more timely manner.

**TABLE<sup>9</sup>**

<b>Rule</b>	<b>Summary Description of Rule</b>	<b>Entities Affected by the Changes</b>
<b>AFFECTED FUNDS (INCLUDING BDCS, REGISTERED CEFS AND INTERVAL FUNDS)</b>		
<b>Registration Provisions</b>		
General Instruction F.4.a of Form N-2	Requires online posting of information incorporated by reference.	Affected Funds
Securities Act Rules 424 and 497	Provide the processes for filing prospectus supplements. Under the Amendments, Rule 424 is the exclusive rule for Affected Funds to file a prospectus supplement (other than an advertisement deemed to be a Rule 482 prospectus).	Affected Funds
Investment Company Act Rule 23c-3	Subjects Interval Funds to the registration fee payment system based on annual net sales.	Interval Funds
Securities Act Rule 486	Allows continuously offered unlisted Affected Funds to make certain filings that are immediately effective upon filing or automatically effective 60 days after filing.	Continuously offered unlisted Affected Funds not relying on Rule 23c-3
General Instruction G of Form N-14	Permits certain registrants to incorporate by reference.	BDCs
<b>Communication Provisions</b>		
Securities Act Rule 134	The Amendments allow Affected Funds to rely on Rule 134, which permits issuers to publish factual information about the issuer or the offering, including “tombstone ads.”	Affected Funds
Securities Act Rule 163A	The Amendments allow Affected Funds to rely on Rule 163A, which permits issuers to communicate without risk of violating the gun-jumping provisions until 30 days prior to filing a registration statement.	Affected Funds
Securities Act Rules 168 and 169	Permit the publication and dissemination of regularly released factual and forward-looking information. The Amendments allow Affected Funds that are reporting companies to rely on Rule 168 and allow Affected Funds to rely on Rule 169.	Affected Funds

<sup>9</sup> Some of the rule changes reflected in this table as applying to “Seasoned Funds” will apply only to Seasoned Funds that elect to file a registration statement on Form N-2, relying on an instruction permitting funds to use the form to file a short-form registration statement.

<b>Rule</b>	<b>Summary Description of Rule</b>	<b>Entities Affected by the Changes</b>
Securities Act Rules 164 and 433	The Amendments allow Affected Funds to rely on Rules 164 and 433 to use a “free writing prospectus.”	Affected Funds
<b><i>Prospectus Delivery Provisions</i></b>		
Securities Act Rules 172 and 173	Permit issuers, brokers and dealers to satisfy final prospectus delivery obligations if certain conditions are satisfied. The Amendments remove the exclusion for Affected Funds.	Affected Funds
<b><i>Periodic Reporting Provisions</i></b>		
Investment Company Act Rule 8b-16	Requires that funds that rely on paragraph (b) of the rule disclose certain enumerated changes in the annual report in enough detail to allow investors to understand each change and how it may affect the fund, including the fund's current investment objectives, investment policies and principal risks, even if no changes have been made in the past year. This requirement is intended to ensure that an investor can access in one location current information regarding these important aspects of the fund.	Registered CEFs
Instruction 4.g. to Item 24 of Form N-2	Requires narrative disclosure about the fund's performance in its annual report.	Registered CEFs
Item 4 of Form N-2; Instruction 10 to Item 24 of Form N-2	Requires disclosure of certain financial information.	BDCs
<b><i>Structured Data Reporting Requirements</i></b>		
Structured Financial Statement Data	Requires that BDCs tag their financial statements using Inline XBRL format.	BDCs
Prospectus Structured Data Requirements	Requires that registrants tag certain information required by Form N-2 using Inline XBRL.	Affected Funds
Form 24F-2 Structured Format	Requires that filings on Form 24F-2 be submitted in a structured format.	Form 24F-2 filers, including open-end funds and unit investment trusts
<b>SEASONED FUNDS<sup>10</sup></b>		
<b><i>Registration Provisions</i></b>		
Securities Act Rule 415	Permits registration of securities to be offered on a delayed or continuous basis.	Seasoned Funds

<sup>10</sup> Seasoned Funds are defined in the Adopting Release as Affected Funds that are current and timely in their reporting and therefore generally eligible to file a short-form registration statement if they have at least \$75 million in “public float.”



<b>Rule</b>	<b>Summary Description of Rule</b>	<b>Entities Affected by the Changes</b>
General Instructions A.2 and F.3 of Form N-2	Provide for backward and forward incorporation by reference for eligible Affected Funds.	Seasoned Funds
Securities Act Rule 430B	Permits certain issuers to omit certain information from their prospectuses at effectiveness.	Seasoned Funds
Securities Act Rule 418	Exempts some registrants from an obligation to furnish certain engineering, management or similar reports.	Seasoned Funds
Regulation FD Rule 103	Provides that a failure to make a public disclosure required solely by Rule 100 of Regulation FD will not disqualify a “seasoned” issuer from use of certain forms.	Seasoned Funds
Securities Act Rule 138	Permits a broker or dealer to publish or distribute certain research about securities other than those they are distributing. The Amendments add a reference to Form N-2 to clarify that Affected Funds that are seasoned are covered by this rule.	Seasoned Funds
<b>PROXY STATEMENTS</b>		
Item 13 of Schedule 14A	Permits certain registrants to use incorporation by reference to provide information that otherwise must be furnished with certain types of proxy statements.	Seasoned Funds
<b><i>Periodic Reporting Provisions</i></b>		
Instruction 4.h.(2) to Item 24 of Form N-2	Requires information about the costs and expenses in the registrant’s annual report.	Seasoned Funds
Instruction 4.h.(3) to Item 24 of Form N-2	Requires information about the share price of the registrant’s stock and any premium or discount in the registrant’s annual report.	Seasoned Funds
Instruction 4.h.(1) to Item 24 of Form N-2	Requires information about each of a fund’s classes of senior securities in the registrant’s annual report.	Seasoned Funds
Instruction 4.h.(4) to Item 24 of Form N-2	Requires disclosure of outstanding material unresolved staff comments that remain unresolved for a substantial period of time.	Seasoned Funds
<b>WKSIs</b>		
<b>Registration Provisions</b>		
Securities Act Rule 462	Provides for effectiveness of registration statements immediately upon filing with the SEC. The Amendments permit Affected Funds that qualify as WKSIs to rely on Securities Act Rule 462.	WKSIs

<b>Communication Provisions</b>		
Securities Act Rule 163	Permits oral and written communications by WKSIs at any time. The Amendments make this available to Registered CEFs that are WKSIs.	WKSIs
<b>ETPs</b>		
<b>Registration Provisions</b>		
Securities Act Rules 415, 424, 456 and 457; Forms S-1, S-3, F-1 and F-3	Permits ETPs to register an undetermined amount of certain securities and pay registration fees based on annual net sales.	ETPs

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