

# THE FINANCIAL SERVICES ROUNDTABLE



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June 22, 2005

Mr. Jonathan G. Katz  
Secretary  
Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

Re: "Definition of Eligible Portfolio Company under the Investment Company Act of 1940,"  
SEC Release No. IC-26647; File No. S7-37-04

Dear Mr. Katz:

The Financial Services Roundtable is pleased to offer its comments on the above-captioned proposed rule by the Securities and Exchange Commission (the "Commission" or the "SEC"), which would change the definition of "eligible portfolio company" for purposes of eligible investments for business development companies ("BDCs"). The proposed eligible portfolio company definition would include private companies and those listed on the Pink Sheets and Over-the-Counter Bulletin Board. It would also include companies listed on an Exchange or NASDAQ, but only if they do not meet the quantitative listing requirements of that market, and they do not meet the initial listing requirements for any other Exchange or NASDAQ.

Small companies face unique challenges in their ability to access capital. The Roundtable is concerned that the proposal, if adopted, would be unduly restrictive and preclude some deserving small and developing companies from receiving BDC financing necessary for their growth. The Roundtable suggests that there are other ways a rule could be crafted to better capture the scope of small or developing companies in need of financing and promote capital formation.

Rather than use a definition of eligible portfolio company based upon which trading platform a stock is traded, a market capitalization standard is an appropriate way to determine the threshold of those public companies in which a BDC could invest. Such a standard can be used and still meet the aims of the Small Business Investment Incentive Act of 1980 ("SBIIA"), which was enacted by Congress to help make capital more readily available to small developing or financing troubled businesses. A \$250 million market capitalization threshold seems appropriate when compared to the legislative history of the SBIIA, which identifies the number of potential eligible portfolio companies to be about 2/3 or 8,000 of all publicly traded companies in 1980.

Market capitalization is an accepted industry and regulatory standard. The SEC uses a market capitalization standard for other rules or orders, such as exemptive orders granting smaller companies additional time to comply with Section 404 of the Sarbanes-Oxley Act. Another example is the SEC's Securities Offering Reform Proposal, which proposes using a \$700 million market capitalization threshold to determine which companies are "well-followed." Industry frequently uses market capitalization to designate different categories of mutual funds or indexes. For example, Standard & Poor's uses market capitalization for several of its indexes, such as the S&P 500 (market capitalization of \$4 billion or more), the S&P MidCap 400 (market capitalization of \$1 billion to \$4 billion), and the S&P SmallCap 600 (market capitalization \$300 million to \$1 billion). It is also very common for the mutual fund industry to use market capitalization of the underlying companies, typically delineated by small-, mid-, and large-capitalization stocks, for mutual funds.

The Roundtable also views the current regulatory uncertainty as untenable. The SBIIA generally defines eligible portfolio companies as those that do not have a class of marginable securities. The margin rules have changed dramatically since the SBIIA was enacted in 1980, such as the 1998 Federal Reserve Board amendments that expanded the definition of margin security to include all securities that trade on the NASDAQ National Market System. This change resulted in a significant reduction in the number of public companies in which a BDC could invest. Moreover, we understand that SEC staff has raised questions as to whether non-public companies with outstanding debt securities may no longer qualify as eligible portfolio companies since debt securities may be marginable. This has created much uncertainty for BDCs and a chilling effect on the capital raising process for small companies seeking BDC financing.

The Roundtable is concerned that the Commission's proposed definition of eligible portfolio company is overly restrictive. The proposed rule would limit the ability of some small and developing companies from receiving capital from BDCs, an important alternative for companies in need of financing. It does not recognize that both private companies and publicly traded companies, regardless of where their stock may trade, may face problems accessing capital. Therefore we urge the Commission to adopt a market capitalization standard to ensure that all companies in need of capital are eligible to receive BDC financing.

We welcome the opportunity to discuss these issues with the Commissioners and staff. If you have any questions or comments on this matter, please do not hesitate to contact me or John Beccia at (202) 289-4322.

Sincerely,

*Richard M. Whiting*

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Executive Director and General Counsel