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United States Government Accountability Office
Washington, DC 20548

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June 3, 2008

The Honorable Christopher J. Dodd
Chairman
The Honorable Richard C. Shelby
Ranking Minority Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable John D. Dingell
Chairman
The Honorable Joe Barton
Ranking Minority Member
Committee on Energy and Commerce
House of Representatives

Subject: *Securities and Exchange Commission: Definition of Eligible Portfolio Company Under the Investment Company Act of 1940*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Securities and Exchange Commission (Commission), entitled "Definition of Eligible Portfolio Company Under the Investment Company Act of 1940" (RIN: 3235-AJ31). We received the rule on May 15, 2008. It was published in the *Federal Register* as a final rule on May 20, 2008. 73 Fed. Reg. 29,044. The final rule has an effective date of July 21, 2008. 73 Fed. Reg. 29,045.

The Commission explained that the final rule amends Rule 2a-46 under the Investment Company Act of 1940 (Act) to more closely align the definition of eligible portfolio company, and the investment activities of business development companies (BDCs), with the purpose that Congress intended. A BDC is a closed-end investment company that Congress established for the purpose of making capital more readily available to certain types of companies. Under the Act, a BDC must invest at least 70 percent of its assets in "eligible portfolio company" securities and certain other securities. The final rule expands the definition of eligible portfolio company to include certain companies that list their securities on a national securities exchange. More specifically, the final rule expands the definition to include Exchange-listed companies that have less than \$250 million in market capitalization.

Enclosed is our assessment of the Commission's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review indicates that the Commission complied with the applicable requirements.

If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Michael R. Volpe, Assistant General Counsel, at (202) 512-8236.

signed

Robert J. Cramer
Associate General Counsel

Enclosure

cc: Nancy M. Morris
Secretary, Securities and
Exchange Commission

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"DEFINITION OF ELIGIBLE PORTFOLIO COMPANY
UNDER THE INVESTMENT COMPANY ACT OF 1940"
(RIN: 3235-AJ31)

(i) Cost-benefit analysis

The Commission conducted a cost-benefit analysis. The Office of Economic Analysis calculated that 7,711 companies, representing 78 percent of public domestic operating companies, qualify as eligible portfolio companies under the amended rule. With respect to costs, the Commission states that, although the amended rule might impose certain administrative compliance costs on BDCs, these costs are similar to the types of compliance costs that a BDC currently undertakes when it invests in a company. Specifically, a BDC will need to determine, prior to investing in a company, if the company has a class of securities listed on an Exchange and whether that company's market capitalization was less than \$250 million as of a date within 60 days prior to the date of the BDC's investment. The Commission notes that costs in obtaining this information will be minimal. The Commission also anticipates that the amended rule will impose only minimal costs on portfolio companies.

(ii) Agency actions relevant to the Regulatory Flexibility Act, 5 U.S.C. §§ 603-605, 607, and 609

The Commission prepared a Final Regulatory Flexibility Analysis under the Act. The Commission here notes that the amended rule will expand the definition of eligible portfolio company to include any domestic operating company with a class of securities listed on an Exchange that has a market capitalization of less than \$250 million. These companies may need BDC financing for continued growth and development, but notwithstanding the fact that their securities are listed on an Exchange, may find it difficult to raise additional capital in new offerings or borrow money through other conventional sources.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the Commission is not subject to the Act.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 et seq.

The final rule was issued using the notice and comment procedures found at 5 U.S.C. § 553. The amendments to Rule 2a-46 were proposed on October 31, 2006, in Definition of Eligible Portfolio Company under the Investment Company Act of 1940, 71 Fed. Reg. 64,093. The Commission received letters from fifteen commenters in response to the proposal. The Commission responds to those comments in the final rule.

Paperwork Reduction Act, 44 U.S.C. §§ 3501-3520

The Commission stated that this final rule does not contain any new or modified information collection requirements subject to the Act.

Statutory authorization for the rule

The Commission promulgated this final rule under sections 2(a)(46)(C)(iv) and 38(a) of the Investment Company Act. 15 U.S.C. §§ 80a-1, 80a-34(d), 80a-37, and 80a-39.

Executive Order No. 12,866

As an independent regulatory agency, the Commission is not subject to the review requirements of the Order.

Executive Order No. 13,132 (Federalism)

As an independent regulatory agency, the Commission is not subject to the review requirements of the Order.