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May 30, 2007

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Definition of Eligible Portfolio Company under the Investment Company Act of 1940; File Number S7-37-04

Dear Ms. Morris:

Representatives of the business development company (BDC) community recently met with the staff of the Division of Investment Management and the Office of Economic Analysis to discuss the pending rulemaking proposal to modernize the definition of "eligible portfolio company" and offered to provide additional information that would be helpful as the Commission works to finalize a rule. We are submitting this comment letter to provide certain additional requested data and to support some of the points made during our discussion regarding the characteristics of exchange-traded companies that have market capitalizations of less than $250 million and the appropriateness of extending the definition of eligible portfolio company to encompass such companies.

The proposed rule suggests two different market capitalization standards for determining which public companies should be treated as eligible portfolio companies for BDC investment purposes. We understand that the use of a market capitalization standard is intended to serve as a proxy for delineating those public companies that tend to already have meaningful access to the public capital markets (through debt or equity issuances) from those that do not. It is the same approach, although for different purposes, that the Commission used in creating a definition to differentiate public companies that are seasoned or well-seasoned issuers from those that are not for purposes of securities offering reform. (Securities Offering Reform, 70 Fed. Reg. 44722 (August 3, 2005) (codified at 17 C.F.R. pts. 200, 228, 229, 230, 239, 240, 243, 249, and 274).

The Commission's securities offering reform effort sought to eliminate unnecessary and outmoded restrictions on offerings, and provide more timely investment information to investors without mandating delays in the offering process that would be inconsistent with the needs of issuers for timely access to capital. The Commission believed that issuers with a demonstrated market following should be subject to different rules than those with less of a following. A market capitalization standard was adopted to identify those companies that have a wide following among market participants, the media, and institutional investors who would be eligible for greater communications and registration flexibilities than for less-followed issuers. The Commission examined data to describe certain characteristics of companies based on market capitalization to describe a universe of companies that generally had a wide market following.

In the pending rule regarding the definition of eligible portfolio company the Commission invited public comment on what size standard would best align the definition with the original purpose Congress intended, including focusing BDC investments in companies that otherwise have difficulty accessing the public capital markets. There are a number of characteristics that evidence the ability, or inability, of a public company to access public capital markets:

- First, those characteristics that help define market following for purposes of offering reform are helpful here as well. Companies that do not have sufficient market following and who are little known to the investing community will have greater difficulty in accessing the market. Therefore, average daily trading volume, institutional ownership, and analyst coverage data based on market capitalization are relevant characteristics to examine. The public comment file contains overwhelming evidence that companies with less than $250 million market capitalization do not have any meaningful market following.

- Second, examining issuer data to determine which companies are currently accessing the capital markets offers additional insight on what market capitalization level would be appropriate in defining eligible portfolio companies. Companies that demonstrate the capacity to issue follow–on equity financings or debt securities are not likely in need of BDC financing (and in fact would likely obtain capital from a lower cost and less intrusive provider than a BDC). We previously submitted data that demonstrates that companies with less than $250 million in market capitalization do not issue any significant amounts of follow-on equity or debt securities.

- Third, looking at generally accepted market indexes is probative of the size of public companies that would tend to have more difficulty accessing the capital markets. Companies that are identified as either micro-cap or small-cap are generally described as companies that have less liquidity and are riskier investments. They also are considered smaller and potentially growing companies that are the intended targets of BDC financing. Again, the public comment file contains significant information that demonstrates that companies with less than $250 million in market capitalization easily fall within the generally accepted and used definition of these market categories.

We are now submitting four additional sets of data that add further weight to the appropriateness of adopting a $250 million market capitalization standard:

- First, we are providing information and data on the current investment portfolios of BDCs to describe the size of their portfolio companies. This data demonstrates that BDC investments in non-exchange traded companies have similar characteristics to exchange-listed companies with market capitalizations of less than $250 million. In addition, this data is responsive to the request for submissions addressing potential concerns that BDCs would invest in larger versus smaller companies under a $250 million market capitalization threshold.

- Second, we are providing additional information and data demonstrating that market participants that provide public capital are not serving the needs of companies with market capitalizations of less than $250 million, and instead are focusing on issuances that are larger than those that can typically accommodate companies of that size.

- Third, we are providing data on the earnings attributes of companies based on market capitalization levels. Earnings are one of the most significant factors that determine the amount of debt or follow-on equity that a company can support. The data demonstrates that companies with market capitalizations of less than $250 million do not tend to have the earnings to support the minimum sizes of capital infusions being offered by institutional capital providers.

- Fourth, in response to the request of Commission staff, we are providing data on the need for capital by companies with market capitalizations of less than $250 million. This data demonstrates that these companies have a need for additional capital.

No approach to define a category of public companies that includes companies that are small, growing, and financially challenged will ever produce a perfect result. The use of a market capitalization standard, as suggested in the proposed rule, cannot insure the perfect demarcation between and among companies, but it is a method that is easy to administer and can be calibrated to serve its intended general purpose. Therefore, in approaching the issue it is important to determine whether it is more prudent to strive to be conservative and potentially under-inclusive, or to be more expansive and potentially over-inclusive. In the instant case if the threshold is set too low it may preclude certain public companies and their shareholders from obtaining capital from a business development company (BDC), as either a lower-cost provider or as the only capital provider. Federal securities laws typically are not designed to impede efficient capital formation. On the other hand, if the threshold is set higher and includes one or more companies that either do not need capital, or that already have access to more traditional forms and less expensive capital, capital formation is not impacted whatsoever. This is because companies, private and public, will generally tend to find the least expensive and least intrusive capital providers. Therefore, we urge the Commission to approach its rulemaking with a predisposition to be more expansive rather than less, and to rely on the capital markets to best decide the proper allocation of capital and credit.

The comment file, including the data submitted below evidences the significant need for capital and the lack of traditional forms of public capital for public companies with market capitalizations of less than $250 million.

1. CURRENT BDC INVESTMENT PORTFOLIOS

BDCs by their design deploy capital they raise in the public markets to a diverse universe of portfolio companies. Today, even the largest BDCs do not make many individual investments of greater than $100 or $150 million. Attached is the most recent consolidated schedule of investments for five of the larger BDCs. Chart 1 below describes the total number of portfolio company investments made by these BDCs and the number of such investments that exceeds $100 million. This data confirms that even the largest BDCs generally focus the majority of their investments in amount of less than $100 to $150 million. As discussed more below, institutional investors do not focus significant efforts in providing capital in such amounts. Therefore, making BDC financing available to such companies is consistent with the BDC-intended mission.

Chart 1
BDC investments by size

	No. of Portfolio Companies	No. of Investments >$100M
Allied Capital [1]	144	9
American Capital[2]	188	14[3]
Apollo Investment[4]	54	0
Ares Capital[5]	60	0
MCG Capital[6]	83	2

We understand that one concern that has arisen in finalizing this rulemaking is a concern that a BDC will focus its resources on the largest eligible portfolio company at the expense of a lesser-capitalized public company. As described in more detail below, the evidence suggests that such is not the case today, and would not be an anticipated result by adopting a $250 million market capitalization standard.

The investment focus of BDCs is well documented by well known and reputable research reports. Below is a chart that describes the investment focus of some of the largest BDCs as described in their Commission filings (Forms N2s and 10Qs). The investment targets that are described encompass a wide spectrum of portfolio company sizes. In addition, the most recent consolidated schedule of investments filed by each BDC describes the current BDC portfolios as encompassing an extensive and broad array of small and middle market companies.

[1] Allied Capital Annual Report for FY 2006.
[2] American Capital Strategies, Ltd., Annual Report for FY 2006.
[3] American Capital Strategies Investor Relations (http://www.acas.com/our_portfolio.html?sort=financing).
[4] Apollo Investment Corporation 10-Q 2006 4Q Filing.
[5] Ares Capital 10-K FY 2006.
[6] MCG Capital Corporation, Annual Report for FY 2006.

Chart 2
INVESTMENT FOCUS

BDC	Investment Focus
American Capital Strategies, Ltd	"We provide investment capital primarily to middle market companies, which we generally consider to be companies with sales between $10 million and $750 million. ... Currently, we will invest up to $800 million in a single middle market transaction in North America."
Allied Capital Corp	"We use the term middle market to include companies with annual revenues typically between $50 million and $500 million."
Apollo Investment Corp	"Our targeted investment typically ranges between $20 million and $150 million, although this investment size may vary proportionately as the size of our capital base changes. In this prospectus, we typically use the term 'middle-market' to refer to companies with annual revenues between $50 million and $1 billion."
Ares Capital Corp	"We primarily invest in first and second lien senior loans and long-term mezzanine debt. In some cases, we may also receive warrants or options in connection with our debt investments. Our investments have generally ranged between $10 million and $50 million each, although the investment sizes may be more or less than the targeted range and are expected to grow with our capital availability. We also, to a lesser extent, make equity investments in private middle market companies. These investments are generally less than $10 million each (but may grow with our capital availability) and are usually made in conjunction with loans we make to these companies."
MCG Capital Corp	"We make debt and equity investments primarily in companies with annual revenue of $20 million to $200 million and earnings before interest, taxes, depreciation and amortization ("EBITDA") of $3 million to $25 million, which we refer to as "middle market" companies.".

Under current law, BDCs can invest in a non-exchange traded company without regard to any size limitation. Therefore, the fact that the current portfolio holdings of BDCs contain companies of both smaller and larger size evidences that BDCs do not simply look for larger company investments.

2. CURRENT CAPITAL MARKET CONDITIONS

In today's market, there is a bias towards larger financings in the leveraged loan and high yield markets – the markets that are the focus of BDC debt investments. This focus is a result of the need to satisfy the return expectations of BDC shareholders. As described in the public comment file, debt of companies with market capitalizations of less than $250 million, including those between $150 million and $250 million in market capitalization, are overwhelmingly rated as below investment grade. Thus, focusing on the capital market conditions of leveraged loans and high yield debt securities will describe the opportunity for companies with market capitalizations of less than $250 million to access the debt markets.

The equity markets focus on public companies with liquidity. One significant measure of liquidity is the average daily trading volume of a company's shares. Shares of companies with market capitalizations of less than $250 million are thinly traded. Thus, these companies do not have any significant access to the equity markets. The data already in the public comment file demonstrates that companies of this size rarely issue follow-on equity financings.

Over the last number of years there has been an evolution in the capital markets that has resulted in institutional investors seeking ever larger and ever more liquid investments. The result is that middle market companies are finding it increasingly more difficult to access institutional capital because such capital is being made available in transaction amounts that exceed what middle market companies can typically support. This is a financing space in which BDCs can and do efficiently operate – for the benefit of the shareholders of BDCs and the owners/shareholders of the portfolio company.

The data in Charts 3 and 4 below demonstrates that institutional capital providers have moved away from serving the segment of the market that needs capital infusions of less than $100 million. In fact, the data clearly shows that institutional capital providers are focused on transactions that average in excess of $300 million.

Chart 3

Average institutional leveraged loan size[7]

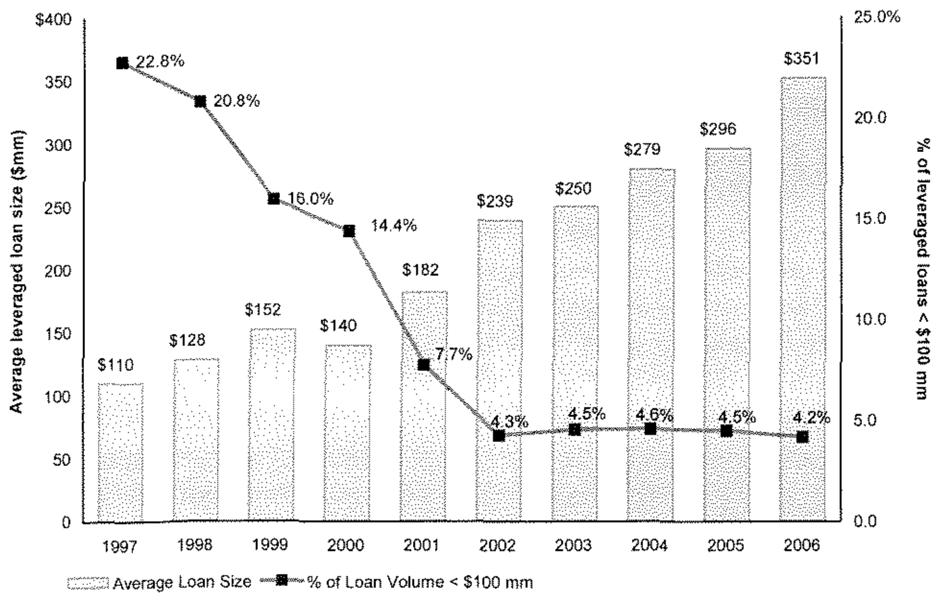


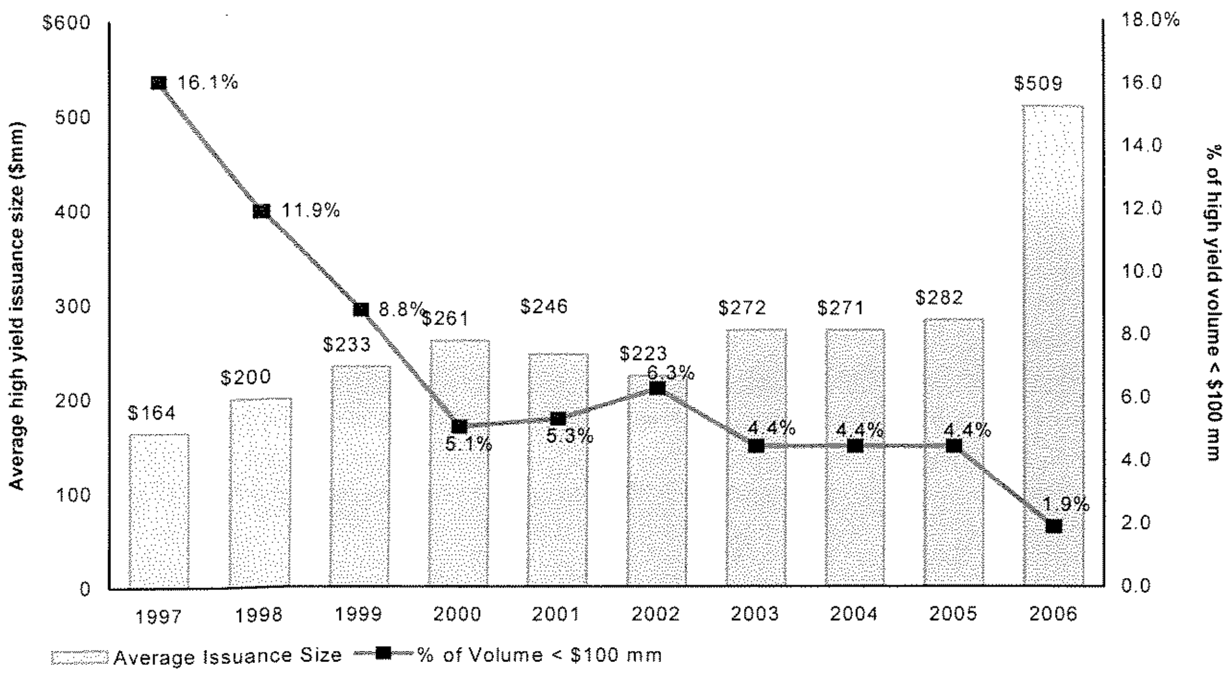
Chart 3 shows that the percentage of institutional leveraged loans that are made for less than $100 million has decreased by more than 75% since 2000 (from 14.4% to

[7] Source: Standard & Poor's
Note: Data through 12/31/06.
Includes loans priced at ≥ LIBOR + 225bps

4.2% of all such loans). In addition, the average loan size has steadily increased, from $140 million to $351 million over this short period.

A similar change has occurred in the average high yield issuance size[8] as shown in Chart 4. Six years ago the average high yield debt issuance was $261 million. By 2006 the average high yield loan was $509 million. In 2000, 5.1% of such loans were for less than $100 million, today that percentage is a mere 1.9%.

Chart 4
Average high yield issuance size



While we did not collect data as far back as 1981, the first year that BDCs appeared, the two charts above describe the dramatic decline in the percentage of capital made available in amounts of less than $100 million for the period beginning in 1997. In 1997, 22.8% of institutional leveraged loans were issued for less than $100 million, compared to only 4.2% figure today. And in 1997, 16.1% of high yield issuances were for less than $100 million, compared to 1.9% today.

In summary, the focus of traditional capital providers is for ever larger and larger transaction sizes. Unless a public company with a market capitalization of $250 million or less has the revenue to support additional capital infusions of more than $100 million

[8] The data previously submitted on debt issuance for all public companies with market capitalizations of less than $250 million demonstrates that to the extent such companies are able to obtain debt financing from the public market, such debt is high-yield. The chart of the high-yield debt issuance thus reflects the credit markets that companies of less than $250 million in market capitalization can potentially access.

at a time, they are unlikely to be able to access public capital from traditional institutional providers. Below is a description of the earnings and revenue streams evidencing that public companies of this size cannot generally support such transactions.

3. MIDDLE MARKET PROFILE

Investors do not make investment decisions based on market capitalization levels *per se*. The most critical factors used in analyzing an investment opportunity are a company's earnings and revenues.[9] Public companies of less than $250 million in market capitalizations simply do not have the revenues to support the average transaction size made by institutional lenders (see above).

The data in Chart 5 below shows that more than half the companies with market capitalizations of less than $250 million have revenues of less than $86 million. The average earnings of all such public companies were just slightly more than $200 million, with 71 companies having revenues in excess of $500 million. These are not revenue levels that would generally support debt amounts in excess of $100 million, or offer attractive returns to obtain additional equity investment.

Chart 5

U.S. Companies with Equity Market Capitalization between $50-$250 Million

Category	No. of	LTM Revenue ($MM)		No. of Companies		Avg. Daily Volume - Last Year (000's of shares)	
(Mkt Cap in $MM):	Companies	Median	Avg.	with Revenue > $500MM		Median	Avg.
$200 - $250 MM	202	$86.1	$207.9	18	8.9%	60.0	158.4
$150 - $200 MM	278	$67.5	$203.6	22	7.9%	43.0	138.8
$100 - $150 MM	360	$43.3	$144.5	22	6.1%	27.0	111.1
$50 - $100 MM	575	$28.4	$74.0	9	1.6%	13.0	62.8
Total	**1,415**	**$45.3**	**$136.5**	**71**	**5.0%**	**26.5**	**103.6**

Source: Capital IQ. Data as of April 20, 2007.

(a) Includes U.S. companies with reported revenue greater than $5.0 million listed on the AMEX, NASDAQ, NYSE or traded OTCBB or OTCPK.

The shares of these companies also were thinly traded – a characteristic that means follow-on public offerings are not likely an option for raising additional capital. These companies had a median daily trading volume of 26,500 shares. Even for the largest of these companies (those between $150 million and $250 million in market capitalizations), the median daily trading volume was less than 60,000 shares.

[9] The comment file is replete with comment letters from BDCs that indicate that adopting a $250 million market capitalization standard will not result in an emphasis on investments in larger cap companies versus smaller cap ones. The reason is that the characteristics that drive investment decisions are earnings and revenue, compared to enterprise value and debt ratios, not market capitalization. Today, BDCs invest in smaller and middle market companies that are not exchange listed based on a company's financials, not size. Whether a company is traded on an exchange or not, the investment analysis by a BDC contemplating an investment will not be different.

Below in Chart 6 is a description of the portfolio companies of three of the largest BDCs accumulated from public filings. This data shows that the average revenue for their portfolio companies was consistent with the revenue and EBITDA of public companies with market capitalizations of $250 million or less.

CHART 6
Portfolio Company Profiles of Leading BDCs
Analysis of Underlying Portfolio Companies[10]

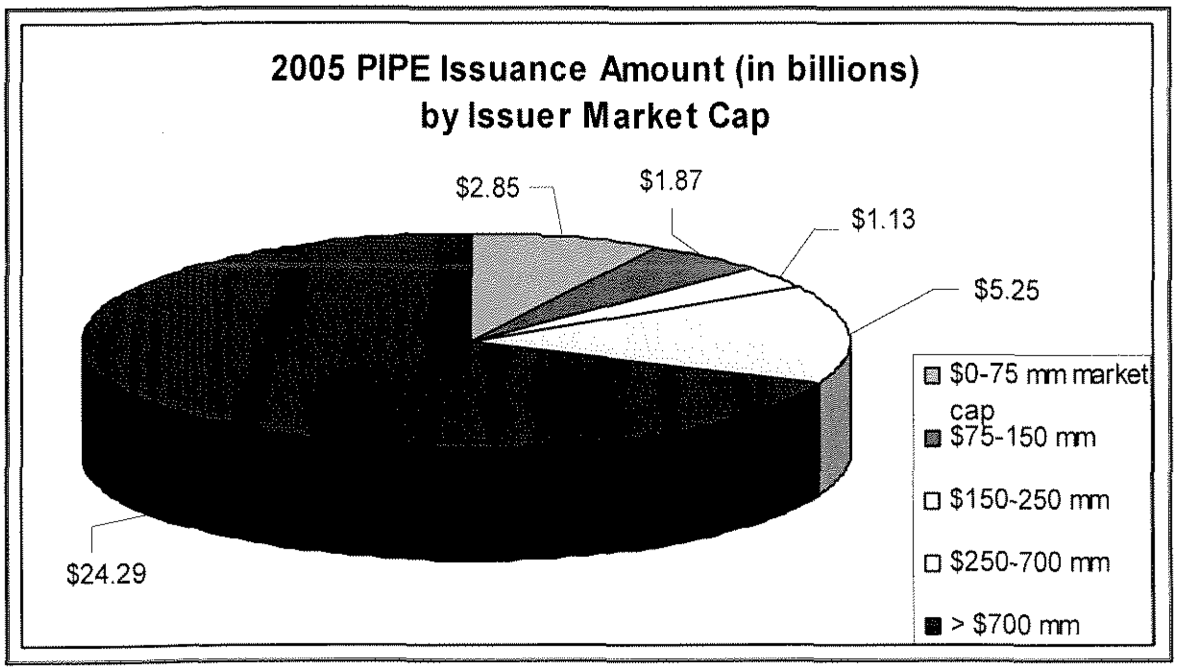
Business Development Company	No. of Portfolio Companies	Average Portfolio Company 2006 Revenue ($millions)
Apollo Investment Corporation (AINV)[11]	46	$397
American Capital Strategies (ACAS)[12]	188	$166
Allied Capital (ALD)[13]	145	$90
MCG Capital[14]	83	$103.3

4. DEMAND FOR CAPITAL

There is no data set that we are aware of to demonstrate the total demand side of capital by smaller public companies. This is true for companies with market capitalizations of less than $150 million as it is for those of less than $250 million. However, there is data that demonstrates that there is enormous demand, even if the total magnitude cannot be measured, for additional capital for these public companies.

In 2005, over $5.85 billion in private investments in public companies (PIPE) financings were entered into by public companies with market capitalizations below $250 million.[15] The approximate 400 public companies between $150 million and $250 million in market capitalization raised $1.13 billion in just a single year (2005) in PIPE financings. This figure demonstrates a significant demand for capital from non-traditional funding sources for companies of this size.

[10] This chart was developed by using the aggregate estimated revenue divided by the total number of portfolio companies. The average is not a published calculation and thus may not be exact with respect to any of the companies listed.
[11] Source: AIC internal analysis / estimates. Based on portfolio holdings as of March 31, 2007.
[12] Source: American Capital Strategies 2006 10-K filing.
[13] Source: Allied Capital Fourth Quarter 2006 Investor Presentation.
[14] Source: MCG Capital Corporation, Annual Report for FY 2006.
[15] Brophy, David J., Ouimet, Paige Parker and Sialm, Clemens, "PIPE Dreams? The Performance of Companies Issuing Equity Privately" (December 10, 2004). EFMA 2004 Basel Meetings Paper



Issuer Market Capitalization	PIPE Issuance
< $75 MM	$2.85 Billion
$75MM - $150MM	$1.87 Billion
$150MM- $250MM	$1.13 Billion
Total 0 - $250 MM	$5.85 Billion
$250MM - $700MM	$5.25 Billion
> $700MM	$24.29 Billion

CONCLUSION

Again, we appreciate the Commission staff meeting with the BDC community to discuss the status of the Commission's efforts to modernize the definition of eligible portfolio company. We hope that this submission responds fully to the suggestions that some additional data sets and analysis would be helpful in completing this rulemaking exercise. We continue to believe that the public comment file contains significant data that supports a $250 million market capitalization standard. We also continue to believe that there is no data that supports distinguishing those companies with market capitalizations below $150 million from those with levels between $150 million and $250 million.

We are happy to provide any additional information that the Commission would find helpful.

Sincerely,

David A. Starr