

Congress of the United States
Washington, DC 20515

February 9, 2022

Chair Gary Gensler
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chair Gensler:

We write today to urge you and your staff to make permanent the exemptive relief that allows business development companies (BDCs) and their affiliates flexibility to participate in certain “follow-on” co-investments (the “Follow-On Relief”).¹ The Commission originally granted the Follow-On Relief to BDCs in April 2020, at the onset of the COVID-19 pandemic, and your staff extended it through no-action positions in January 2021 and March 2021. Absent further action, the Follow-On Relief will expire at the end March 2022.²

We see strong policy grounds for making the Follow-On Relief permanent. In fact, BDCs and their Main Street investors could suffer harm if the Follow-On Relief expires. We encourage you and your staff to act expeditiously to make the Follow-On Relief permanent or, at a minimum, to extend it for a significant period of time.

Anecdotally, we have learned from a number of BDCs that the Follow-On Relief has been critical to their operations in light of the economic downturn caused by the pandemic. We have been informed that the Follow-On Relief has allowed the deployment of at least nearly \$2 billion of additional capital to BDC portfolio companies to help them weather the pandemic by strengthening their balance sheets and supporting their organic growth opportunities, without materially undermining investor protections.

The additional capital has allowed BDCs to pursue their underlying statutory mandate – laid out by Congress when BDCs were created in 1980 – to support smaller and medium-sized U.S. businesses. These small and medium-sized businesses, often referred to as the “middle

¹ SEC Order Granting Exemptions From Specified Provisions of the Investment Company Act and Rules Thereunder; Release No. IC-33837 (Apr. 8, 2020); *See also SEC Provides Temporary, Conditional Relief for Business Development Companies Making Investments in Small and Medium-sized Businesses* (Apr. 8, 2020), <https://www.sec.gov/news/press-release/2020-84>.

² *See Division of Investment Management Responses to Frequently Asked Questions, Question III.1, Temporary additional flexibility for BDCs* (“Until March 31, 2022, the Division will not recommend enforcement action to the SEC, to the extent that any BDC with an existing co-investment order continues to engage in transactions described in Section III of the BDC temporary order, pursuant to the same terms and conditions described in that section. This statement updates the Division’s position of January 5, 2021, by extending the expiration date of the staff position from March 31, 2021 to March 31, 2022.”)

market,” have limited access to capital and other conventional forms of financing, such as bank loans. Unlike private funds, banks, and other investment companies, BDCs are statutorily mandated to support U.S. middle market businesses, because they are required to invest 70% of their assets in privately-owned U.S. operating companies or public U.S. companies with a market capitalization of less than \$250 million, and to offer significant managerial assistance to the companies in which they invest.

If your staff does not make the Follow-On Relief permanent, or at a minimum extend it for a significant period, a BDC is restricted from participating in “follow on” co-investments with certain of its affiliates, even if the BDC has applied for and received from the Commission an individualized exemptive order allowing it to participate in other types of co-investments. These exemptive orders typically permit a BDC to co-invest alongside a private fund and then to make subsequent investments in the same portfolio company with the same private fund – but do not allow any other private fund affiliate to make such subsequent investment. The Follow-On Relief allows a BDC to participate in a follow-on co-investment in a portfolio company alongside an affiliated private fund that did not originally participate in the initial investment, subject to the existing terms and conditions in each fund’s exemptive order, as well as BDC board oversight.

Without the Follow-On Relief, that affiliated private fund would be prevented from supporting a BDC’s bid by offering its own capital – and the portfolio company will often look to other lenders able to finance its entire need. As a practical reality, many private funds have limited terms, and “successor” private funds take their place. The Follow-On Relief allows these successors and other private fund affiliates to support a BDC’s bid when the original private fund no longer exists or is otherwise unable to do so.

The Investment Company Act of 1940 provides important protections designed to prevent a BDC manager and its affiliates from overreaching relative to the BDC. In the circumstance of allowing new private funds to participate in a follow on co-investment opportunity, those investor protection concerns are not implicated because the opportunity for overreach is negligible, if at all. The Follow-On Relief does not, for example, permit a private fund to buy out the BDC’s interest, which could raise valuation and other concerns. Nor does the Follow-On Relief allow an affiliate of the BDC to dump its position on the BDC, one of the key concerns leading to the enactment of the Investment Company Act of 1940. The private funds in the follow-on transaction are not the subject of the protections under the Act. Instead, the participation of a new private fund in a follow-on offering can provide crucial new capital support to the company, which can protect the BDC’s investment.

Beyond the need for an extension specifically of the Follow-On Relief, we also believe the broader regulatory regime governing BDCs and other investment company co-investments is in need of modernization. We share the Commission’s goal of protecting BDC and investment company shareholders, but the reliance by the Commission on a patchwork of individually-granted, highly technical, and confusing exemptive orders unnecessarily impinges on BDC investors. The ability to co-invest generally provides BDCs and their investors with a host of benefits, including an increase in deal flow, the opportunity to participate in larger financing commitments with enhanced selectivity, and more favorable deal terms. But the process for

exemptive orders often preclude BDCs from participating in these opportunities, which ultimately is a detriment to Main Street investors and Main Street businesses, alike. This frustrates the purpose Congress assigned to BDCs – to promote investment in and to provide growth capital to smaller and growing U.S. businesses.

While we believe a broader reform is needed, we remain primarily focused on the imminent expiration of the temporary Follow-On Relief in March 2022. We urge you to make the Follow-On Relief permanent, or at a minimum to extend the relief for a significant period of time. Such action would benefit of BDCs and their shareholders, as well as the Main Street businesses that they support.

Sincerely,



Gwen Moore
Member of Congress



Bryan Steil
Member of Congress

CC: William A. Birdthistle, Director, Division of Investment Management
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