



April 14, 2017

Submitted electronically to submissions@banking.senate.gov

The Honorable Mike Crapo
Chairman
Senate Committee on Banking, Housing,
and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Sherrod Brown
Ranking Member
Senate Committee on Banking, Housing,
and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

RE: Request for Proposals to Foster Economic Growth

Dear Chairman Crapo and Ranking Member Brown,

Thank you for your commitment to promoting economic growth and enabling consumers, market participants and financial companies to better participate in the economy. CNL Financial Group is a private investment management firm specializing in alternative investment products. Anchored by over 40 years of thoughtful investing in relationships, CNL Financial Group or its affiliates have formed or acquired companies with more than \$33 billion in assets. Performance-driven, CNL Financial Group strives to achieve investment returns by identifying emerging trends, accessing capital through its national distribution channels, and investing shareholder capital in a variety of credit and real estate investment products. Over its history, CNL Financial Group has invested through various market cycles in a broad range of industries, asset classes and geographies. Through our wholly owned subsidiaries, we advise Corporate Capital Trust ("CCT") and Corporate Capital Trust II ("CCT II") which are both externally managed, non-diversified closed-end investment companies that have elected to be regulated as Business Development Companies, or BDCs, under the Investment Company Act of 1940. As of our most recently filed financial statements, CCT and CCT II have over 70,000 shareholders, and currently have approximately \$4B invested in nearly 150 U.S. companies across 34 states. Together, the U.S. companies in which CCT and CCT 2 are invested, support approximately one million employees. We are also a member of the Investment Program Association (IPA). We fully support the IPA submission of three legislative proposals to the Committee related to business development companies, in which you can find greater detail about the issues addressed in this letter, along with suggested legislative text. We appreciate your solicitation of ideas from the public, and it is our privilege to submit to the Committee three policy recommendations.

BDCs serve a crucial role in the U.S. economy through their dedication to investing in small and midsize U.S. businesses. In fact, BDCs are statutorily required to invest at least 70% of their assets in small and midsize domestic companies, a segment of the economy we commonly refer to as the "middle market." According to the National Center for the Middle Market, the U.S. middle market

represents 33% of private sector GDP and one-third of all U.S. jobs.¹ Employment growth at middle market firms consistently outpaced that of large corporations and small businesses over the past five years and is estimated to be responsible for three out of five net new private-sector jobs.²

At least partly in recognition of the importance of BDCs in financing the middle market, the House Financial Services Committee voted 53-4 in favor of the “Small Business Credit Availability Act” (H.R.3868) in the 114th Congress. That bill contained five substantive provisions aimed at modernizing the regulation of BDCs. We write today to express our strong support for two of the provisions in H.R.3868, namely: (1) the provision to implement offering reforms that would put BDCs back on a level footing with companies that received relief under the 2005 securities reforms; and (2) the provision that would provide a modest increase in leverage limits from 1:1 to 2:1. Legislative text for these changes is included as “Addendum A” as part of the IPA’s submission to the Committee.

We also write in support of a third proposal that would put BDCs on level-footing with mutual funds and real estate investment trusts (“REITs”) by permitting BDCs to offer multiple classes of common stock to investors. Not only would this change put BDCs on a level playing field with mutual funds and REITs, it is a key component of the ability of BDCs to comply with the Department of Labor’s Conflict of Interest Rule (“Fiduciary Rule”). Legislative text for this regulatory change is included in “Addendum B” of the IPA’s submission to the Committee.

Parity for Business Development Companies Regarding Offering and Proxy Rules

In 2005, the Securities and Exchange Commission (“SEC”) adopted final rules relating to Securities Offering Reform, which were the most sweeping liberalization and modernization of the registered offering process under the Securities Act of 1933 Act (the “Securities Act”) in decades. Unfortunately, the majority of these updates did not apply to BDCs. At the time the rule revisions were implemented, the SEC indicated it would consider reforms for BDCs at a later date, but this has not happened. This package of reforms, Section 4 of H.R.3868, would make up for that oversight by directing the SEC to revise certain rules to allow BDCs to use streamlined securities offering provisions available to all other registrants under the Securities Act, such as Well-Known Seasoned Issuer status and incorporation by reference. These amendments will reduce burdensome, duplicative regulatory paperwork for BDCs, while still ensuring investors receive relevant and necessary disclosures. In addition, the amendments will grant eligible BDCs greater flexibility and efficiency in raising capital by allowing them to time offerings for when they will be best received by the market.

This set of simple and modest reforms would benefit both BDC shareholders, the small- and medium-sized business in which they invest and, in turn, have a positive impact on economic growth by decreasing the cost and increasing the efficiency of capital formation for BDCs. Every other type of public company in America that registers under the Securities Act benefits from streamlined rules

¹ National Center for the Middle Market; 4Q 2016 Middle Market Indicator.

² *Id.* “Five years of MMI data consistently show the middle market producing jobs one-and-a-half or two times faster than either big or small business.”

reflecting the electronic age. BDCs and their shareholders should have access to the same streamlined filing benefits.

Expanding Access to Capital for Business Development Companies

Section 3(a)(2) of H.R.3868 would reduce the asset coverage ratio requirement applicable to BDCs from 200% to 150% if certain conditions are met. Reducing the asset coverage ratio would grant BDCs a modest increase in borrowing capacity, or leverage. It is important to note that this proposal would not codify an immediate increase in the leverage ratio for every BDC. On the contrary, the proposal would require a majority of the independent directors of a BDC to authorize the new asset coverage ratio and then delay the effective date of such change for one year (“cooling off period”), unless a majority of the shareholders vote to adopt such change immediately. For a non-traded BDC, after the board or general partner vote to take advantage of the new asset coverage ratio, the non-traded BDC must offer to redeem (buy back) the shares of 100% of its shareholders over the course of the one year cooling off period at a rate of 25% per quarter.

The demand for growth capital by middle market firms continues to increase, with 65% of middle market respondents seeking to invest in their business in the coming year.³ In the wake of reduced bank lending to this segment of the economy following the financial crisis, the middle market has increasingly turned to BDCs for growth capital and routine financing. This proposal would directly and positively impact economic growth by increasing BDCs’ ability to meet the capital needs of small and midsize U.S. businesses.

Allowing the Issuance of Multiple Classes of Common Stock by Business Development Companies

This proposal, which would allow BDCs to issue more than one class of common stock, would provide more flexibility for BDC investors, while putting BDCs on level-footing with mutual funds and REITs. Furthermore, this change is a key component of the ability of BDCs to comply with the Fiduciary Rule.

Permitting BDCs to issue multiple share classes would enhance investor choice. Investors would benefit from a menu of options from which to choose regarding how to invest in a BDC, thereby empowering the investor to select the manner of purchasing shares that the investor deems most appropriate for his or her particular circumstances, such as the amount of the purchase, the length of time the investor expects to hold the shares or existing relationships with financial advisors.

Additionally, the ability to issue multiple share classes would expand the ability of BDCs to lend to small and mid-market U.S. businesses by placing them on a level playing field with mutual funds, REITs and registered closed-end funds, which are currently permitted to issue multiple classes of shares. Finally, the ability of BDCs to issue multiple classes of shares will become a practical

³ *Id.*



necessity upon the implementation of the Fiduciary Rule. The Fiduciary Rule will necessitate that covered issuers be able to offer at least two share classes: one designed for distribution by “Level Fee Fiduciaries,” and one designed for distribution under the Best Interest Contract Exemption. Mutual funds, closed-end funds and REITs will find themselves well positioned for the post-Fiduciary Rule marketplace, but BDCs will be at a considerable disadvantage without the requested change.

We thank you for the opportunity to submit these legislative proposals for consideration by the Senate Banking Committee. We share your commitment to fostering economic growth and increasing economic participation. We believe BDCs have been working toward these goals since their creation by Congress in 1980, and we hope the legislative proposals we submit today will amplify our effectiveness in both regards.

Respectfully,

A handwritten signature in blue ink that reads "Thomas K. Sittima".

Thomas K. Sittima
Chief Executive Officer
CNL Financial Group