

under the ICOS Order. Under the new rule, the board of directors of an R&D company relying on the rule's safe harbor must adopt and record a resolution that the company is primarily engaged in a non-investment business⁵⁶ and adopt a written investment policy.⁵⁷

Although we have identified certain costs and benefits that may result from the new rule, rule 3a-8 is exemptive, rather than prescriptive, and R&D companies are not required to rely on it. Therefore, we assume that R&D companies will rely on the rule only if the anticipated benefit from doing so exceeds the anticipated cost. In the Proposing Release, we requested comment and specific data regarding the costs and benefits of the proposed rule. We did not receive any comments or data regarding the costs and benefits of the rule from commenters.

A. Benefits

The Commission expects rule 3a-8 to benefit R&D companies in a number of ways. As mentioned, the new rule affords R&D companies greater flexibility to both raise and invest capital than currently allowed. The requirement under the ICOS Order that an R&D company's research and development expenses equal or exceed gross investment revenues, in effect, imposed a "burn rate," requiring the R&D company to spend the income from and the principal amount of its investments in its research and development business. As a result of these limitations, R&D companies may have forgone opportunities to access the markets or may have reduced the amounts raised when accessing the markets. These limits also may have discouraged investment in higher yielding capital preservation instruments. The rule allows R&D companies to raise larger amounts of capital in a more cost-effective manner and to formulate more efficient asset allocations than is permitted under the existing tests. Thus, the rule should reduce any costs that may be associated with a lack of flexibility (1) to access fully the markets when conditions are favorable, and (2) to make capital preservation investments.

Furthermore, by clarifying the extent to which R&D companies may make investments in other companies pursuant to collaborative research and development arrangements, rule 3a-8 will provide R&D companies increased certainty as to the amount of these investments they may make without

becoming subject to regulation under the Act. The Commission anticipates that this will reduce costs on an ongoing basis. When an R&D company's status under the Act is uncertain, it may experience higher costs when issuing securities or when borrowing. The Commission expects clarification of the test to both reduce the costs that an R&D company may need to incur to determine its status under the Act and reduce any uncertainty in such determination, which may reduce costs when issuing securities or borrowing.

B. Costs

R&D companies that choose to rely on the new rule's nonexclusive safe harbor will incur certain costs in complying with the rule's conditions that are not currently imposed under the ICOS Order. The rule requires an R&D company's board of directors to adopt and record a resolution that the company is primarily engaged in a non-investment business and also to adopt a written investment policy concerning the company's capital preservation investments. Because these requirements need to be fulfilled only once, the Commission believes the cost of the requirements to be minimal relative to the benefits provided by the safe harbor. We estimate that to comply with the requirement that the board of directors adopt and record a resolution, and R&D company would need to have its in-house counsel spend 45 minutes preparing the resolution, and its board of directors spend 15 minutes adopting the resolution. We expect the board of directors to have based its decision to adopt the resolution, in part, on investment guidelines the R&D company has established to ensure its investment portfolio is in compliance with the rule's requirements.⁵⁸ We therefore believe that no additional time will be required for the board of directors to formally adopt a written investment policy, as required by the rule, along with the resolution. Based on our estimate that 500 companies will rely on the rule, one hour per company at a blended hourly rate results in a total costs of \$103,750.⁵⁹ In the Proposing

⁵⁸ We believe that many of the companies that will seek to rely on the rule already have written investment guidelines.

⁵⁹ The Commission's estimate concerning the weighted average hourly wage rate is based on salary information for the securities industry compiled by the Securities Industry Association. See Securities Industry Association, Report on Management & Professional Earnings in the Securities Industry—2001. The weighted average hourly wage rate of \$207.50 includes overhead costs and assumes that 75 percent of the time will be by in-house counsel at a rate of \$110 per hour and 25 percent by the board of directors at a rate of \$500 per hour.

Release, the Commission solicited comment on the number of companies that may rely on the rule, the amount of time needed to adopt the required resolution and the costs of such time. We did not receive any comments on our estimates.

IV. Consideration of Promotion of Efficiency, Competition, and Capital Formation

Section 2(c) of the Act provides that whenever the Commission is engaged in rulemaking under the Act and is required to consider or determine whether an action is consistent with the public interest, the Commission also must consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. The Commission believes that, by clarifying the status of certain R&D companies under the Act, and allowing R&D companies greater flexibility to raise and invest capital, the rule is consistent with the public interest and will positively affect capital formation. The Commission also believes that the rule will promote efficiency and competition, and that the rule will not be unduly burdensome to those companies wishing to rely on it. In the Proposing Release, the Commission solicited comments on this section, but did not receive any.

V. Paperwork Reduction Act

New rule 3a-8 requires R&D companies wishing to rely on the safe harbor provided under the rule to fulfill a number of conditions. Certain of these conditions constitute "collections of information" within the meaning of the Paperwork Reduction Act of 1995 ("PRA") [44 U.S.C. 3501 *et seq.*]. One condition is that the board of directors of the company adopt an appropriate resolution evidencing that the company is primarily engaged in a business other than that of investing, reinvesting, owning, holding, or trading in securities. The rule requires that the resolution be recorded contemporaneously in the company's minute books or comparable documents. The Commission submitted this collection of information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The title for the collection of information is "Rule 3a-8 under the Investment Company Act." OMB has approved the collection of information for rule 3a-8; the OMB control number is 3235-0574 (expires March 31, 2006).

In the Proposing Release, the Commission estimated that the total

⁵⁶ Rule 3a-8(a)(6)(iv).

⁵⁷ See Proposing Release, *supra* note 3, at III.A.4.b.