



March 30, 2009



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LETTER OF COMMENT NO.

Via Email

Technical Director, Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

File Reference: Proposed FSP FAS 157-e

We appreciate the opportunity to provide our comments to the Board regarding Proposed FSP FAS 157-e. By way of background, Ares Capital Corporation ("ARCC") is a Business Development Company ("BDC") regulated under the Investment Company Act of 1940 (the "'40 Act"). BDCs are publicly traded, closed-end investment funds that provide capital, usually in the form of loans, to small and middle market businesses. Congress created BDCs in 1980 (in response to difficult market conditions akin to those we are currently experiencing) to increase the flow of capital through public market vehicles to companies that would otherwise have limited access to financing. As such, BDCs act as commercial lenders that provide growth and acquisition financing like banks and commercial finance companies.

Request for Amortized Cost Approach for Hold to Maturity BDC Assets and Reopening of FAS 159 Window for BDC Liabilities

Unlike other publicly held closed-end funds or mutual funds, BDCs do not invest in traded securities. Instead, BDCs privately negotiate direct loans and investments in operating companies with maturities typically ranging from five to seven years. We view these loans as illiquid since they are non-registered and include few, if any, other lenders. These loans are smaller issues to small borrowers in situations where there is limited to no public information or market making.

As a company regulated under the '40 Act, ARCC is required to value its assets on a quarterly and annual basis under the guidelines of FAS 157. As it is currently interpreted, FAS 157 requires a mark to market approach, despite the private illiquid nature of our assets. Given the dramatic dislocation in the credit markets, the application of FAS 157 to BDCs in its current form has had a negative impact on the industry's ability to raise capital in the public and private markets, which in turn decreases liquidity to U.S. middle market companies. By contrast, banks and commercial finance companies, which hold similar, and sometimes even the same assets, use a hold to maturity approach (amortized cost less credit impairment reserve).

Even when applying FAS 157, we believe that our assets should be valued under the hold to maturity approach since fair value measurement per FAS 157 requires determination of

a price to sell the asset "in the principal (or most advantageous market) for the asset". Given that there is no principal market for us to sell the asset, the most advantageous market would be a refinancing of the loan through a merger or acquisition involving the issuer, where a performing loan is typically repaid at par.

Along with other BDCs, ARCC requests that the FASB use its authority to permit BDCs to value their fully performing loans which are intended to be held to maturity at amortized cost. This would parallel the accounting treatment available to banks and commercial finance companies holding similar assets.

In addition, we also request that the FASB consider reopening the window for the fair value option for financial liabilities under FAS 159. The original window closed prior to the market dislocation, and as such many BDCs did not make this election. There now exists an imbalance between how the value of assets and liabilities are currently being assessed. Specifically, net asset values are distorted as BDC liabilities are being valued at cost, whereas BDC assets are valued on a mark to market basis. The differences are particularly acute in a market where interest rate volatility and the lack of liquidity has impacted both asset and liability values. Furthermore, this misclassification has serious ramifications for the BDC industry as it struggles with the already difficult challenges of financial covenant compliance with lenders.

Specific Comments on Proposed FSP FAS 157-e

Although we believe that amortized cost less reserves for credit impairment is the best approach to valuing our assets, we plan to continue to apply FAS 157 as currently interpreted using the mark to market approach. As you can appreciate, all parties (including our outside valuation providers and auditors) struggle to apply the mark to market approach given the inactive and dislocated markets within which we operate.

While we believe the guidance provided in the proposed FSP FAS 157-e is helpful as it relates to defining inactive markets and distressed transactions, we believe there are additional considerations that the FASB should take into account, and we would request additional guidance on certain critical issues.

Inactive Markets

We agree with the seven factors provided in paragraph 11 under "Step 1" to indicate that a market is not active, and would recommend adding one additional factor: "the market has few participants relative to historic standards". As discussed above, we hold assets that are illiquid by nature and for which there are no (nor have there ever been) trading markets. The only effective "market" in which we participate is the new issue origination market comprised of a bi-lateral agreement between ourselves as lender and middle market companies as borrowers. The manner in which we "exit" these loans is typically upon repayment from a refinancing or in an M&A transaction.

Appropriate Discount Rates in Utilizing the Income Approach

As is our current practice, after determining that a market is inactive or a transaction is distressed, we will use a discounted cash flow or a "bond yield" approach in determining valuation for our performing loan assets. However, we seek clarity on what is an appropriate discount rate.

We believe that the new Example 11 and particularly paragraph A32F are a step in the right direction. The midpoint utilized by Entity A is illuminating, but we would like further clarity or examples of how one would set the range of required returns for our assets, which are comprised of privately negotiated loans and notes in private, middle market companies (as compared to the example on collateralized debt obligations).

As we read paragraph A32F we understand that the 7% is based upon returns in a "hypothetical active market" and 15% is based upon "bid-level yields implied". For our asset classes, we would view a required return from a "hypothetical active market" based upon rates demanded for originated middle market loans over a historic period of time (such as the previous five to 10 years) when the origination market was active. Using an average discount rate derived from a longer time period would more closely match the typical holding period for discounting the cash flows of such assets, and smooth out expected returns over a business cycle. This would place less weight on price talk for originated deals in the current, inactive credit environment. We would view "bid-level yields implied" as current or recent pricing (actual or discussed in the market) on primary middle market transactions, notwithstanding the current credit dislocation. We would ask that FASB consider these definitions when the concepts of a "hypothetical active market" and "bid-level yields implied" are applied to the illiquid lending arena in which we operate

Thank you for your consideration.

Sincerely,



Richard Davis
Chief Financial Officer
Ares Capital Corporation

cc: Mary Schapiro, Chairman
Securities and Exchange Commission