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Douglas J. Scheidt
Associate Director and Chief Counsel
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Dear Mr Scheidt

Ark Therapeutics Group plc

We are writing on behalf of our client, Ark Therapeutics Group plc ("**Ark**"), an emerging healthcare group that is organized as a public limited company under the laws of England and Wales. We are of the view that Ark is a research and development company meeting the requirements of Rule 3a-8 ("**Rule 3a-8**") under the Investment Company Act of 1940 (the "**Act**"), and that its proposed investments in: (a) shares of international money market funds ("**IMMFs**"); (b) certificates of deposit ("**CDs**") of US and non-US financial institutions; (c) term deposits ("**Term Deposits**") held with US and non-US financial institutions; (d) US and non-US investment-grade commercial paper ("**CP**"); and (e) US and UK government obligations, all as described herein (the "**Proposed Investments**") and in accordance with the written investment policy attached as Schedule A hereto (the "**Investment Policy**"), should be treated as capital preservation investments and not other investments within the meaning of Rule 3a-8¹ and that, accordingly, Ark will not become an investment company within the meaning of the Act by investing in the Proposed Investments. We request the concurrence of the staff of the Division of Investment Management (the "**Staff**") of the Securities and Exchange Commission (the "**Commission**") with our view that the Proposed Investments should be treated as capital preservation investments for purposes of Rule 3a-8(b)(4).

1. BACKGROUND

Ark is a holding company with four direct and indirect wholly-owned subsidiaries: (a) Ark Therapeutics Limited, a limited company organized under the laws of England and Wales ("**ATL**"); (b) Ark Therapeutics Oy, a corporation organized under the laws of Finland ("**ATO**"); (c) KerraTec Inc., a Delaware corporation ("**KerraTec**"); and (d) Patient Plus Limited, a limited company organized under the laws of England and Wales ("**PPL**"). The principal activities of Ark's subsidiaries are the research and development of healthcare products targeted at specific unmet clinical needs within vascular disease and cancer and the commercialization of such products. As discussed in more detail in paragraph 3.2 below, Ark has one product introduced into hospitals and three further lead products in late stage clinical development.

¹ Rule 3a-8(b)(4) defines the term capital preservation investment as "an investment that is made to conserve liquidity until the funds are used in the issuer's primary business or businesses" and Rule 3a-8(b)(8) defines the term other investment as "an investment in securities that is not a capital preservation investment".

As discussed in paragraph 4.1 below, Ark is currently not required to be registered as an investment company within the meaning of Section 3(a)(1) of the Act.² Ark would like to rely on the non-exclusive safe harbor exemption from registration under the Act provided to research and development companies ("**R&D Companies**") pursuant to Rule 3a-8. Ark is an R&D Company and complies with the requirements set forth in Rule 3a-8(a)(1)–(3) and (5)–(6). Accordingly, Ark does not ask the Staff to consider any issues arising under these individual subparagraphs.

Although Ark is not engaged in the business of investing, reinvesting or trading in securities, Ark would like to invest its liquid assets, including the proceeds of the Offer (as defined in paragraph 3.1 below), in some or all of the Proposed Investments, as it deems most advantageous, in order to support its healthcare product business, in particular its continuing research and development programs (the "**R&D Programs**"). In order to comply with Rule 3a-8(a)(7) under the Act, the Board of Directors of Ark has adopted the Investment Policy.

In order to comply with Rule 3a-8, the Proposed Investments must fall within the definition of capital preservation investments or, if not, be subject to percentage limit requirements with respect to other investments.³ The adopting release for Rule 3a-8 (the "**Adopting Release**"),⁴ however, does not specify objective criteria for classifying an investment as a capital preservation investment. In analyzing whether an investment should be categorized as a capital preservation investment, many R&D Companies look to the investment policies adopted by ICOS Corporation and Corvis Corporation, and reviewed by the Staff in connection with the issuance of the ICOS Order⁵ and the Corvis Order⁶ (as more fully discussed in paragraph 4.3 below), for guidance. As both ICOS Corporation and Corvis Corporation are US companies, their investment policies only included certain types of securities that are denominated in a currency other than the US dollar ("**Non-US Securities**"). Presumably, those securities would be available and typically used by non-US R&D Companies in their cash management activities.

Additional guidance for non-US R&D Companies as to these matters is lacking. Rule 3a-8 does not differentiate between US and non-US R&D Companies; nor does it set forth a list of specific instruments that fall within the definition of capital preservation investments or prescribe the permitted issuers or currency of denomination of such investments. In the Adopting Release, the Commission, in response to a commentator's comment suggesting that the Commission define capital preservation investments using specific objective standards, stated that it believed that "attempting to specify such objective criteria would render the rule unnecessarily complex and inflexible" and that not providing such criteria was appropriate given the variety of circumstances that an R&D Company may face.⁷ Thus, in adopting Rule 3a-8 and declining to provide specific guidance regarding the definition of capital preservation investments, the Commission opted for providing R&D Companies with the flexibility they need to operate their business in a non-speculative manner. Within this context, absent a more specific definition of capital preservation investment, a non-US R&D Company such as Ark should have the flexibility to invest in instruments that are available and customarily used by R&D Companies in their relevant jurisdiction to conserve capital and liquidity if they present limited credit risk. The Proposed

² Section 3(a)(1)(A) of the Act defines the term investment company to mean "any issuer which is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities". Section 3(a)(1)(C) of the Act defines the term investment company to mean any issuer which "is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities, and owns or proposes to acquire investment securities having a value of exceeding 40 per centum of the value of such issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis".

³ See Rule 3a-8(a)(4).

⁴ See Certain Research and Development Companies, Investment Company Act Release No. 26077 (June 16, 2003), which became effective on August 19, 2003.

⁵ ICOS Corporation, Investment Company Act Release Nos. 19274 (February 18, 1993) (notice) and 19334 (March 16, 1993) (order granting exemption) (the "**ICOS Order**").

⁶ Corvis Corporation, Investment Company Act Release Nos. 25774 (October 21, 2002) (notice) and 25804 (November 18, 2002) (order granting exemption) (the "**Corvis Order**").

⁷ See the Adopting Release, *supra* note 4, at II.D.1.i.

Investments, including the Non-US Securities, are readily available and customarily used in Ark's jurisdiction of incorporation, the UK, to manage liquidity and preserve capital. Ark currently intends that most of its Proposed Investments will be denominated in pounds, Ark's functional currency and the currency in which it incurs most of its expenses, rather than dollars, so as to minimize the risk of exchange rate fluctuations.

Ark believes that its Investment Policy should allow it to meet its objectives of preserving principal and maintaining a diversified portfolio, while minimizing credit risk and maximizing yield, by enabling it to invest in instruments, the Proposed Investments, that are designed to conserve capital and liquidity and present limited credit risk pending Ark's use of such funds in its primary business, and that are available and customarily used in the UK, Ark's jurisdiction of incorporation and the location of its senior management.

Based on the guidance provided by the Commission in the Adopting Release, the precedents set forth in the ICOS Order and the Corvis Order and the characteristics of the Proposed Investments as discussed in paragraph 4.3 below, on behalf of Ark, we request the concurrence of the Staff with our view that the Proposed Investments should be treated as capital preservation investments and not as other investments for purposes of Rule 3a-8(b)(4).

2. THE ADOPTION OF RULE 3a-8

Before 1993, the main test to determine a company's primary business under Section 3(b)(2) of the Act was the test adopted in *Tonopah*.⁸ In 1993, the Commission issued the ICOS Order⁹ recognizing that the asset and income factors set forth in the *Tonopah* test were having unintended negative consequences on many R&D Companies. In the ICOS Order, the Commission also recognized that many of the instruments in which R&D Companies would invest their capital would be investment securities counted toward the 40% threshold set forth in Section 3(a)(1)(C) of the Act. As a result, R&D Companies might have few assets other than investment securities and *bona fide* R&D Companies would fall within Section 3(a)(1)(C) of the Act's definition of investment company. In the Commission's view, becoming subject to regulation under the Act was incompatible with how operating R&D Companies conduct their business.

In the ICOS Order, the Commission modified the *Tonopah* test for determining the primary business of an R&D Company under Sections 3(b)(1) and 3(b)(2) of the Act. The modified test focuses on three factors relating to the company's use of its income and assets, instead of the composition and sources of those assets. The initial three requirements are whether the company: (a) uses its securities and cash to finance its research and development; (b) has substantial research and development expenses and *de minimis* investment expenses; and (c) invests in securities in a manner consistent with the preservation of its assets until needed to finance operations. If these three initial tests are met, the Commission would then look at the remaining *Tonopah* factors: the company's historical development, its public representations of policy and the activities of its officers and directors.

In May 2002, the Biotechnology Industry Organization ("**BIO**"), which represents more than 950 biotechnology companies in the US and 33 other countries, including 20 members in the UK and two in Finland, petitioned the Commission to promulgate a rule to address the need to further revise the traditional income/asset test set forth in the ICOS Order for determining investment company status. In its proposal (the "**BIO Petition**"),¹⁰ BIO asserted that the biotechnology industry has changed greatly since 1993 and the ICOS Order's test is arbitrary and unduly limiting.

⁸ See *Tonopah Mining Co.*, 26 SEC 426 (1947) ("**Tonopah**"). Under the *Tonopah* test, the Commission looks at a company's historical development, its public representations of policy, the activities of its officers and directors, the nature of its assets and, finally, the sources of its present income. The *Tonopah* test has also been used to determine whether a company satisfies the primary business test under Section 39(b)(1) of the Act.

⁹ See the ICOS Order, *supra* note 5.

¹⁰ *Petition for Investment Company Act of 1940 Rulemaking*, submitted by Matthew A. Chambers and John C. Nagel, Wilmer, Cutler & Pickering, on behalf of the Biotechnology Industry Organization, File No. 4-457 (May 23, 2002).

For example, the ICOS Order does not account for the fact that, with increased frequency, biotechnology companies are investing in joint ventures to perform joint research and development with strategic partners. These joint ventures may include non-controlling interests deemed investment securities under the Act and not fitting the definition of capital preservation investments set forth in the ICOS Order.

In response to the BIO Petition, in November 2002, the Commission proposed¹¹ and, in June 2003 adopted, Rule 3a-8. Rule 3a-8 codifies many of the principles first enumerated in the ICOS Order and provides a non-exclusive safe harbor from the definition of investment company for certain *bona fide* R&D Companies.¹² Rule 3a-8 allows R&D Companies, such as those involved in the biotechnology industry, to have increased flexibility in raising and investing capital for research, development and other operations.

3. **ARK'S OPERATING ACTIVITIES**

3.1 **Overview**

Ark was established in 1997 and, throughout its existence, has been a biotechnology company focused on researching and developing healthcare products to address areas of unmet clinical need in vascular disease and cancer. Healthcare products are subject to lengthy and rigorous pre-clinical testing and clinical trials and other extensive, costly and time-consuming procedures mandated by various regulatory authorities. Ark has a history of operating losses. Like most emerging healthcare companies, Ark has been focused on its R&D Programs and has only recently had one of its products approved for commercial use.

In order to continue to fund its R&D Programs, Ark successfully completed its initial public offering in connection with its listing on the London Stock Exchange (the "**Offer**") on March 3, 2004. The Offer comprised an aggregate of 41,555,999 shares priced at £1.33 per ordinary share (the "**Shares**"), corresponding to a total offer size of approximately £55 million. The Shares were not registered under the US Securities Act of 1933 (the "**Securities Act**"). The Shares were offered and sold outside of the US to non-US persons in reliance on Regulation S under the Securities Act and within the US only to qualified institutional buyers, as defined in and in reliance on Rule 144A under the Securities Act ("**QIBs**"), in transactions exempt from the registration requirements of the Securities Act. As further described in paragraph 4.1 below, upon receiving the proceeds of the Offer, Ark placed them in instant access deposit accounts held with UK banks pending determination or receipt of no-action relief from the Staff with respect to the status of the Proposed Investments outlined in this letter.

3.2 **Operations**

Ark was established by three founding scientists, two of whom are based at University College London ("**UCL**") and one of whom is based at the AI Virtanen Institute at the University of Kuopio, Finland. Each of the three founding scientists continues to play a leading role in Ark's R&D Programs. Ark has research groups in London and in Finland with complementary capabilities. These groups undertake research programs which are interrelated in the overall process of product development. The London-based group researches the biology of the vascular system and its diseases, and the Finland-based group focuses on the area of gene-based medicine and the development of new vectors and delivery systems.

¹¹ See Proposed Rule: Certain Research and Development Companies, Investment Company Act Release No. 25835 (November 26, 2002).

¹² See the Adopting Release, *supra* note 4. The Commission also noted that adoption of Rule 3a-8 does not preclude issuers from continuing to determine their status in accordance with the ICOS Order, *id.*, at footnote 17.

Ark's focus is on product candidates that have the potential for orphan drug status in the US or Europe or for fast track designation from US regulatory authorities. In general, Ark's strategy is to try to retain value by controlling clinical development, manufacture, registration and marketing of its lead products. The clinical evaluation, manufacture and marketing of Ark's products and its ongoing research and development activities are subject to regulation by regulatory and governmental authorities in all territories in which Ark, or any of its partners or licensees, wishes to test, manufacture or market products. The regulatory process is extremely expensive and generally takes many years to complete. Ark generated minimal revenues in 2003 and limited revenues of approximately £150,000 in 2004 attributable to its one marketed product, however, Ark has incurred net losses since its founding. It is uncertain when Ark will become profitable.

(a) **Lead Products, Pipeline Projects and Intellectual Property**

Lead Products. Ark has a portfolio of proprietary healthcare products targeted at specific unmet clinical needs within vascular disease and cancer. Of its four lead products, Ark has one approved product, Kerraboot, which it introduced to hospitals in the UK in November 2003, and three further lead products in late-stage clinical development. Ark's lead products comprise:

- *Kerraboot*, a novel wound dressing device for leg and foot ulcers. It has completed its clinical development and has been approved for marketing in both Europe and the US. Kerraboot generated limited revenues in the last two months of 2003 and in 2004.
- *Cerepro*, a novel gene-based product for the treatment of patients with an operable type of malignant brain tumor, given in addition to standard surgery and radiotherapy/chemotherapy. Cerepro has completed two safety and efficacy studies. Ark is currently preparing an application for European Union ("**EU**") marketing approval based on exceptional circumstances and expects that the necessary materials will be submitted to the regulatory authorities during the first half of 2005.
- *Vitor*, an oral small molecule therapy for the treatment of muscle wasting that occurs in patients with cancer. Ark has commenced a Phase III study due for completion in 2005. Vitor has been awarded fast track designation by the US Food and Drug Administration (the "**FDA**"). Ark currently expects that first filing for EU marketing approval for Vitor will occur in 2005 and filing for US regulatory approval will occur in 2007.
- *Trinam*, a novel gene-based therapy and biodegradable delivery device being developed to prevent the blocking of veins and arteries that frequently occurs after vascular surgery. Trinam is currently in a Phase II study, the initial part of an approved Phase II/III trial, and the FDA has awarded it orphan drug status. Ark currently expects that first filing for EU marketing approval for Trinam will occur in 2007.

At this time, only Kerraboot has been approved for commercial use and, while well progressed, Ark's three unapproved lead products in late-stage clinical development will require additional clinical evaluation, regulatory review, significant marketing efforts and substantial investment before they could provide Ark with any significant revenues. If marketing approval for Cerepro is granted under exceptional circumstances, marketing could commence in late 2005 or in 2006. Otherwise, with the exception of Kerraboot, Ark does not expect to be able to market any of its lead products for a number of years.

Pipeline Projects. Ark's lead products are supported by a pipeline of earlier stage products and technologies in research and pre-clinical development, including a drug targeting technology and a new vector and potential functional genomics platform. In addition, Ark is conducting follow-on R&D Programs based around vascular biology and growth factors. These products and programs are many years away from gaining regulatory approval.

Intellectual Property. Since its inception, Ark has filed 15 families of patent applications claiming inventions which have been generated by Ark's own scientists, as well as through its agreements with its founding scientists and consultants at UCL and the University of Kuopio.

(b) **Manufacturing and Research Facilities and Employees**

Ark's R&D Programs take place mainly in the UK and Finland. Ark has a manufacturing facility in Kuopio, Finland and has upgraded these facilities to be compliant with FDA and European Agency for the Evaluation of Medicinal Products ("**EMEA**") certification requirements for the production of gene-based medicines for Phase III and Phase IV/corroborative studies for further trials of Cerepro and Trinam.

A majority of Ark's employees work in research and development. As at December 31, 2004, Ark had 127 employees and consultants/contract researchers. Of these employees: 16 were involved in research (UK); 69 were involved in research and manufacturing (Finland); 13 were involved in development; 11 were involved in sales and marketing; and 18 were involved in finance and administration. Overall, Ark has a research group of approximately 92 scientists and practicing clinicians, with its biologists, chemists and development teams based in London and its gene science and vector technology teams based in Kuopio, Finland.

3.3 **Financial History**

Ark has experienced operating losses in each year since its inception, with retained losses of £5.7 million, £6.4 million and £12.8 million for the years ended December 31, 2002, 2003 and 2004, respectively. As at December 31, 2004, Ark had an accumulated deficit of approximately £40.5 million. Ark expects to incur further substantial operating losses in its current and future financial years as its research and development activities continue. Ark's historical financial results reflect principally research and development and other administrative expenses. Ark expects that its research and development expenses will increase significantly over the next two years as Ark pursues late-stage clinical trial development of its unapproved lead products and discovery research capabilities are expanded. For the year ended December 31, 2004, Ark's total expenses amounted to £16.2 million. Of these total expenses, £11.5 million, or 71%, were incurred in pounds, the equivalent of £3.8 million, or 23%, were incurred in euros, and the equivalent of £0.9 million, or 6%, were incurred in dollars. Ark's research and development expenses amounted to £9.1 million for that year.

Prior to the Offer, Ark's research and development and other financial requirements were financed primarily through private placements of equity securities. Ark has only received a limited amount of interest income on the proceeds of these private placements. Ark has incurred net losses in each year since its founding, and expects to continue to incur net losses until 2007 and may incur net losses in subsequent periods. In addition, the Listing Particulars, dated March 3, 2004, submitted to the London Stock Exchange in connection with the Offer (the "**Listing Particulars**") stated that Ark intends to use the proceeds of the Offer, along with Ark's existing available cash resources, to continue the development of Ark's products and, in particular, for the following purposes:

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- approximately 51% on the continued development of its lead product candidates, including investment in upgrading its development manufacturing facilities to be compliant with FDA and EMEA certification requirements for the production of gene-based medicines for Phase III and Phase IV/corroborative studies for further trials of Cerepro and Trinam;
- approximately 30% on the commercial launch of, and subsequent sales and marketing for, Kerraboot and other products as they receive marketing approval;
- approximately 13% on other research and development activities; and
- the balance for working capital and other general corporate purposes.

Ark's expectation as to the use of proceeds of the Offer has not materially changed since the publication of the Listing Particulars.

4. **ARK'S STATUS UNDER THE ACT**

4.1 **Section 3(a)(1)**

In general, all companies that satisfy certain statutory criteria based on their asset composition or business activities are defined as investment companies and are required to register and be regulated under the Act, unless an exclusion or exemption is available.

Ark is currently not required to register as an investment company within the meaning of Section 3(a)(1) of the Act.

Ark believes (based on a careful and in-depth inquiry by its chief financial officer, with our assistance, as to its historic development, its public representations and policy, the activities of its officers and directors, the nature of its current assets and investments, the sources of its income and all other factors deemed relevant in accordance with existing precedent) that prior to and following the Offer, and application of the proceeds thereof, it had always been and will continue to be engaged primarily in the business of developing healthcare products and is not, therefore, an investment company as defined in the Act.¹³

In addition, Ark does not own investment securities¹⁴ having a value exceeding 40% of its total assets on an unconsolidated basis.¹⁵

¹³ See Section 3(a)(1)(A) of the Act, *supra* note 2.

¹⁴ See Section 3(a)(1)(A) of the Act, *supra* note 2. For purposes of 40% test described in Section 3(a)(1)(C) of the Act, the term investment securities includes all securities except (a) US government securities, (b) securities issued by employees' securities companies, and (c) securities issued by majority-owned subsidiaries of the issuer which (1) are not investment companies and (2) are not relying on the exception from the definition of investment company in paragraph (1) or (7) of Section 3(c) of the Act.

¹⁵ Ark's assets are almost entirely comprised of cash, together with securities in its wholly-owned direct and indirect subsidiaries, ATL, ATO, PPL and KerraTec, which are themselves not investment companies within the meaning of the Act and, accordingly, such securities are not investment securities for purposes of Section 3(a)(1)(C) of the Act. ATL's assets, other than cash items, are mainly comprised of its investments in ATO, its direct subsidiary, as well as some laboratory and office equipment. Although ATO, too, maintains some cash resources to satisfy its own liquidity requirements, ATO's assets are mainly comprised of machinery and equipment, computers and buildings used in its research and development activities. Both ATL and ATO are principally engaged in research and development, and the commercialization of Ark's products. PPL holds the European rights to commercialize Kerraboot and is exclusively engaged in the selling and marketing of Kerraboot. PPL's principal assets are inventory and some trade debt. KerraTec is a direct subsidiary of Ark that was incorporated for the purpose of commercializing Kerraboot in the US. KerraTec does not have any meaningful assets. For purposes of determining whether Ark may rely on Rule 3a-8, and for purposes of this letter other than the foregoing analysis as to why Ark is not an investment company under Section 3(a)(1)(C) of the Act, Ark has consolidated its financial statements with those of its wholly-owned subsidiaries in accordance with Rule 3a-8(b)(2).

Ark, however, is concerned that it could be deemed to be an investment company under Section 3(a)(1) of the Act if Ark invests in the Proposed Investments and Rule 3a-8 is unavailable. As described in paragraph 3.1 above, the Offer was made outside the US to non-US persons in reliance with Regulation S under the Securities Act and was made in the US only to QIBs in reliance on Rule 144A under the Securities Act. The Offer was not structured to ensure compliance with either Section 3(c)(1) or (7) of the Act.¹⁶

Accordingly, the certification requirements for subsequent transfers of securities sold to US residents in the Offer and other precautionary measures customarily used by issuers to ensure continued compliance with the requirements of Section 3(c)(1) or (7) of the Act were not used in connection with the Offer.¹⁷ In addition, although Shares in the Offer were only sold in the US to QIBs (and restrictions were put in place to ensure that those Shares, within the US, may only be resold to QIBs), there were no requirements that US resident purchasers of the Shares, or their US resident transferees, be qualified purchasers as defined in Section 2(a)(51) of the Act.¹⁸

To preserve its status as a non-investment company pursuant to Section 3(a)(1)(C) of the Act, Ark has invested the proceeds of the Offer (pending their use in financing Ark's R&D Programs) in interest bearing demand deposits (the "**Demand Deposits**") and maintains a substantial majority of its other financial resources in the form of Demand Deposits at Barclays Bank plc, The Royal Bank of Scotland plc and Halifax Bank of Scotland plc, each a non-US bank. In the Hallwood No-Action Letter,¹⁹ the Staff confirmed that interest bearing demand deposits held with non-US banks would be considered "cash" and not counted as investment securities for purposes of the 40% asset test under Section 3(a)(1)(C) of the Act.

If Ark were to transfer the proceeds of the Offer from the Demand Deposits to the Proposed Investments in order to enhance the return from its investment, its status under the Act could be impaired if the Proposed Investments are viewed as investment securities under Section 3(a)(2) of the Act.²⁰ Ark believes that limiting its investment of the

¹⁶ Section 3(c)(1) of the Act exempts from the definition of an investment company any issuer whose outstanding securities are owned by not more than 100 persons and which is not making or proposing to make a public offer of its securities. We are aware that the Staff has taken the position that the exemption provided by Section 3(c)(1) of the Act would be available if there are no more than 100 beneficial owners of the relevant securities resident in the US without taking into account those beneficial owners resident outside the US. See Investment Funds Institute of Canada no-action letter (pub. avail. Mar. 4, 1996). Section 3(c)(7) of the Act exempts from the definition of an investment company any issuer whose outstanding securities are owned exclusively by qualified purchasers and which is not making or proposing to make a public offer of its securities. We are aware that the Staff has taken the position that the exemption provided by Section 3(c)(7) of the Act would be available if all beneficial owners of the relevant securities resident in the US are qualified purchasers without taking into account those beneficial owners resident outside the US. See Goodwin, Procter & Hoar no-action letter (pub. avail. February 28, 1997).

¹⁷ We note that restrictions on the transferability of the Shares would breach the Listing Rules of the UK Listing Authority and would be ineffective in any event, as UK regulations governing the settlement of securities in electronic book-entry form, only permit CRESTCo (the operator of the electronic book-entry securities system in the UK) to refuse to register transfers in very limited circumstances (e.g., because transfer is prohibited pursuant to a court order).

¹⁸ We note that although substantially all QIBs will also be deemed qualified purchasers, pursuant to Rule 2a51-1(g)(1) under the Act there are certain exceptions where a QIB would not also be deemed a qualified purchaser.

¹⁹ Hallwood Industries Incorporated no-action letter (pub. avail. June 19, 1991) (the "**Hallwood No-Action Letter**") (the Staff confirmed that interest bearing demand deposits held at non-US banks or foreign offices or branches of US banks are considered "cash" and not investment securities for purposes of the Act).

²⁰ It is possible that, even if Ark were deemed an investment company for purposes of Section 3(a)(1)(C) of the Act as a result of the Proposed Investments, Ark might still be exempt from registration under the Act pursuant to Section 3(c)(1) of the Act. Ark has not conducted a public offering in the US and, as part of the Offer, its securities were only sold to 16 investor accounts in the US (none of which purchased more than 10% of Ark's outstanding voting securities), or less than 100 US beneficial owners. See Touche Remnant & Co. no-action letter (pub. avail. August 27, 1984) (the "**Touche Remnant No-Action Letter**") and Investment Funds Institute of Canada, *supra* note 16. Although in the Indosuez Asset Management Asia Limited no-action letter (pub. avail. February 14, 1997) the Staff confirmed that a company would not violate Section 7(d) of the Act if the 100 US beneficial owner limit under the Touche Remnant No-Action Letter was exceeded due to the independent action of its securityholders (e.g., the relocation of its non-US securityholders to the US or purchases by US persons of securities in offshore secondary market transactions), Ark prefers not to rely on these no-action positions as (a) it did not impose any restrictions on the number of investors to

proceeds of the Offer and other cash resources to the Demand Deposits or other cash items that are not investment securities for the purpose of Section 3(a)(1)(C) of the Act would limit significantly its ability to manage its healthcare product business, conduct its R&D Programs and increase shareholder value as a result of the comparatively low investment returns such investments offer as compared to the Proposed Investments. By investing its cash resources in the Proposed Investments instead, Ark believes that it will preserve capital and liquidity while avoiding unreasonable risk, thus maximizing the funds available to finance its R&D Programs and enhancing shareholder value.

Ark further believes that it is an R&D Company of the type for the benefit of which Rule 3a-8 was promulgated, and that the Proposed Investments are capital preservation investments within the meaning of Rule 3a-8. For the reasons outlined in the preceding two paragraphs and in section 1 above, Ark would like to rely on the safe harbor provided by Rule 3a-8 as described in more detail below.

4.2 **Rule 3a-8(4)**

In order to comply with Rule 3a-8(a)(4), the Proposed Investments must fall within the definition of capital preservation investments or, if not, be subject to the percentage limit requirements with respect to other investments.²¹

In the Adopting Release, the Commission stated that capital preservation investments are "liquid so that they can be readily sold to support the R&D Company's research and development activities as necessary and present limited credit risk".²² In addition, ". . . investments in equity and speculative debt would not meet the definition of capital preservation investments, but would be considered 'other investments' subject to the limits set forth in the rule".²³ While the Adopting Release makes it clear that investments in "equity or speculative debt" would not be considered capital preservation investments, the Commission declined to specify objective standards for criteria such as the type of issuer, credit quality, maturity, liquidity and currency of capital preservation investments. The Commission has thus allowed R&D Companies to design their investment portfolios in a way that suits their individual needs, while requiring them to evaluate and categorize each individual investment as either a capital preservation investment or an other investment. In paragraph 4.3 below, we describe Ark's Proposed Investments and why we believe they should be categorized as capital preservation investments under Rule 3a-8.

4.3 **Proposed Investments**

Ark would like to invest in the Proposed Investments, including the Non-US Securities, because they are available and customarily used in the UK by R&D companies to conserve capital and liquidity and present limited credit risk while generally having higher returns than the Demand Deposits Ark currently holds. They also provide Ark with a range of permissible investments denominated in the currencies in which it principally incurs its expenses, the pound and the euro, giving it a number of alternative types of securities to consider in choosing an investment portfolio that provides a favorable yield while maintaining credit risk, individual maturities and portfolio duration and diversification within acceptable limits and protecting Ark from the foreign exchange rate risks that would

whom further resales of those securities initially sold in the US could be made, but rather only limited such resales to QIBs, as already described, and (b) it may in the future wish to raise additional funds in the US, through a public offering or otherwise. Ark would instead prefer to rely on the non-exclusive safe harbor provided by Rule 3a-8.

²¹ Rule 3a-8(a)(4) states that an issuer will be deemed not to be an investment company if its investments in securities are capital preservation investments, except that: (a) no more than 10% of the issuer's total assets may consist of other investments or (b) no more than 25% of the issuer's total assets may consist of other investments that are investments made pursuant to a collaborative research and development arrangement.

²² See the Adopting Release, *supra* note 4, at II.D.1.i.

²³ *Id.*

result from investments denominated in US dollars. As described in paragraph 3.3 above, Ark intends to use the Proposed Investments, and the yield therefrom, principally to finance its R&D Programs and not for speculative purposes. With this goal in mind, each of the Proposed Investments will be highly rated by a nationally recognized rating agency, thus presenting limited credit risk, and will be sufficiently marketable and/or short-term to provide the required liquidity. Accordingly, Ark believes that the Proposed Investments discussed below, including the Non-US Securities, are of the type envisaged as capital preservation investments under Rule 3a-8.

We note that the investment policies reviewed by the Commission in connection with issuing the ICOS Order²⁴ and the Corvis Order²⁵ included such investments as certain US government obligations,²⁶ US commercial paper, US bank obligations (including certificates of deposits and term deposits) and US open-end money market funds²⁷ meeting the requirements of Rule 2a-7 under the Act.²⁸ In addition, the liquidity management guidelines of ICOS Corporation permitted investments in certain of the Non-US Securities.²⁹ Although the investment guidelines of Corvis Corporation did not include any of the Non-US Securities or other non-US investments (aside from dollar denominated commercial paper issued by a foreign branch of a US bank),³⁰ and certain of the Proposed

²⁴ See ICOS Order, *supra* note 5.

²⁵ See Corvis Order, *supra* note 6.

²⁶ We note that, for purposes of determining whether a company is an investment company under Section 3(a)(1) of the Act, these US government obligations would not constitute investment securities for purposes of Section 3(a)(1)(C) of the Act by virtue of the operation of Section 3(a)(2) of the Act and the Act's definition of Government securities in Section 2(a)(16).

²⁷ We are aware that, for purposes of determining whether a company is an investment company under Section 3(a)(1) of the Act, the Staff has taken the position that in certain cases these US money market funds would be treated as cash items. See *Willkie Farr & Gallagher* no-action letter (pub. avail. October 23, 2000) (US money market fund shares counted as cash for purposes of investment company status determination) (the "**Willkie No-Action Letter**").

²⁸ See the Corvis Order, *supra* note 6, (the Commission granted an order allowing Corvis to use a portion of its working capital to purchase and hold short-term, investment grade securities, as outlined in its investment policies attached to its application); the ICOS Order, *supra* note 5, (ICOS invested in "high-quality, short-term Government and commercial debt instruments pending their use to fund the company's research and development programs").

²⁹ See ICOS Corporation, Amended and Restated Application for an Order of Exemption pursuant to Section 3(b)(2) of the Investment Company Act of 1940 (filed October 26, 1992), at Exhibit H (the "**ICOS Investment Policy**").

The ICOS Investment Policy stated that investments shall consist of the following types of securities:

Governments/Agencies	Domestic Instruments
US Treasury Bills	Repurchase Agreements
US Gov't Coupon Issue	Bankers Acceptances
Federal Agencies	Commercial/Financial Paper
Foreign Instruments	Master Notes
Euro Certificates of Deposit	Certificates of Deposit
Yankee Certificates of Deposit	Corporate Notes
Bankers Acceptances	Floating/Variable Rate Securities
Commercial Paper	

³⁰ See Corvis Corporation, Amended and Restated Application for an Order under Section 3(b)(2) of the Investment Company Act of 1940 (filed October 18, 2002), at Exhibit 6 (the "**Corvis Investment Policy**").

The Corvis Investment Policy included the following investments:

Commercial Paper – issued by a domestic corporation with a maturity of 90 days or less; **US Treasury Securities** – treasury notes, bills and bonds with remaining maturities not to exceed 18 months; **Bank Obligations** – any certificate of deposit, time deposit, eurodollar CD issued by a foreign branch of a US bank, bankers' acceptance, bank note or letter of credit issued by a US bank; **Repurchase Agreements** – purchased from one of the top 20 banks or one of the primary dealers regulated by the Federal Reserve that is at least 102% collateralized by US Government obligations; **Funds** – any open end money market fund regulated by the US government under Rule 2a-7 under the Act or any investment fund advised by a Registered Investment Advisor under Rule 3c-7, which guidelines must state that the "fund will seek to maintain a US\$1 per share net asset value"; and **US Government Obligations** – any obligation issued or backed (federal agencies) by the US Government with a maturity of 180 days or less.

Investments (such as IMMFS, Term Deposits held with non-US financial institutions and non-US government securities) appeared in neither policy, Ark believes that the Proposed Investments provide the same level of protection and capital preservation as those investments included in the investment policies of ICOS Corporation and Corvis Corporation considered by the Commission prior to implementation of Rule 3a-8 under the ICOS Order and the Corvis Order, respectively.³¹

(a) **International Money Market Funds**

Ark would like the ability to invest in shares of IMMFS that are authorized, and managed by investment advisors authorized and regulated, by a financial regulatory authority in one or more of the following EU member states: Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Spain, Sweden and the United Kingdom ("**Permitted Member States**"), and that are denominated in pounds, euros and/or dollars. IMMFS are mutual funds that invest in short-term highly rated debt instruments, typically including bank deposits, certificates of deposit, commercial paper, floating-rate notes, asset-backed securities, repurchase agreements and short-term corporate and government bonds. These assets are actively managed within very strict investment guidelines adopted by the IMMFS to offer safety of principal, liquidity and competitive returns. Ark would like the ability to invest in IMMFS because their investment return is highly competitive compared to the returns offered by the Demand Deposits and they provide similar liquidity, with same-day or next-day access to funds. Much as with US money market funds meeting the requirements of Rule 2a-7 under the Act, IMMFS, because of the generally higher rates of interest they offer, are used in a manner similar to a bank account for companies with surplus funds for short-term liquidity.

Under the Investment Policy, Ark may only invest in IMMFS that:

- (i) state that their objective is to protect capital and preserve liquidity;
- (ii) have a money market fund rating of at least Aa by Moody's Investors Service ("**Moody's**") or AA by Standard & Poor's ("**S&P**");³²
- (iii) have no more than 5% of their assets invested with any one financial institution or corporate issuer;
- (iv) have a weighted average maturity of 75 days or less;
- (v) have a stable or accumulating net asset value per share;
- (vi) provide same-day or next-day settlement;
- (vii) have assets under management of at least £250 million (or the equivalent in other currencies);
- (viii) are registered as undertakings for collective investments in traded securities ("**UCITS**") under relevant EU directives and legislation of one or more of the Permitted Member States;

³¹ See the ICOS Order, *supra* note 5, and the Corvis Order, *supra* note 6.

³² Money market fund ratings are opinions of the investment quality of shares in the funds and assess the safety of invested principal. Money market funds rated Aa by Moody's are judged to be of high quality by all standards. Similarly, those rated AA by S&P assess that safety is strong and those funds have a "strong capacity to maintain principal value and limit exposure to loss".

- (ix) are authorized by a financial regulatory authority in one or more of the Permitted Member States; and
- (x) are managed by investment advisors authorized and regulated by a financial regulatory authority in one or more of the Permitted Member States.

We believe that the IMMFS would qualify as capital preservation investments within the meaning of Rule 3a-8(b)(4), even though they are not subject to regulation in the US and may invest primarily in debt securities of non-US entities. US money market funds are safe investments because they are regulated and they provide a diversified and professionally managed portfolio of securities, relative safety of principal, a high degree of liquidity and a wide range of shareholder services. The IMMFS will be similar to US money market funds in a number of respects. The Investment Policy contains restrictions with respect to: (a) portfolio maturity (the IMMFS must have a portfolio with a maximum weighted average maturity of 75 days or less); (b) portfolio quality (the IMMFS must have a stated aim of protecting capital and preserving liquidity, and the IMMFS must itself be highly rated); and (c) portfolio diversification (the IMMFS must have no more than 5% of its assets invested with any one entity). In addition, the IMMFS will be required to provide same-day or next-day settlement to help ensure liquidity and must have a stable or accumulating net asset value per share.

Although the IMMFS will not be regulated under Rule 2a-7 of the Act, they will be required to have a money market fund rating of at least Aa by Moody's or AA by S&P. We note that in the absence of Rule 2a-7, the international market initially looked to rating agencies to provide assurance as to the quality of the funds. The criteria applied to IMMFS by the rating agencies are influenced by the requirements of Rule 2a-7. Included in these criteria are such factors as: (a) portfolio quality; (b) portfolio composition, including diversification, weighted average maturity, maximum maturity, liquidity, investments in variable and floating-rate securities and policies regarding securities lending and reverse repos; (c) portfolio and security valuation methods; (d) net asset value deviation procedures; (e) management, including investment policy and philosophy, portfolio management techniques and strategies, internal controls and procedures, personnel and ownership; and (f) the composition of the IMMFS's investor base. In order to obtain a money market fund rating of Aa by Moody's or AA by S&P, a US money market fund would generally need to satisfy more stringent criteria than the requirements of Rule 2a-7 of the Act, including lower weighted average maturity levels and higher credit quality through a portfolio comprised of first tier securities only. Accordingly, IMMFS rated Aa by Moody's or AA by S&P would be subject to more stringent criteria than those of Rule 2a-7 of the Act. These criteria are supported by periodic rating agency inspection and regular review of full details of the IMMFS's portfolio. Indeed, a fund that met the bare minimum requirements of Rule 2a-7 would at best qualify for a money market fund rating of BBB from S&P.³³ Similarly, such a fund would not be able to achieve a money market fund rating of Aa from Moody's.³⁴

The IMMFS will also be authorized by a financial regulatory authority in one or more of the Permitted Member States, and similarly they will be managed by established investment advisors of the kind that provide "a diversified and professionally managed portfolio of securities, relative safety of principal, a high degree of liquidity and a wide range of shareholder services"³⁵ that are authorized and

³³ See Standard & Poor's Money Market Fund Ratings Criteria (2003) at 25 (avail. at www2.standardandpoors.com).

³⁴ See Moody's Taxable Money Market Fund Rating Guidelines.

³⁵ See the Willkie No-Action Letter, *supra* note 27, at page 15.

regulated by a financial regulatory authority in one or more of the Permitted Member States.

Although each Permitted Member State has its own regulatory regime, IMMFs that are registered as UCITS are subject to member state regulation that must, at a minimum, satisfy the requirements of EU directives.³⁶ Under these requirements, each of the IMMf and its manager must be authorized by a financial regulatory authority in a member state. These requirements also include other rules for investor protection including those relating to: (a) portfolio composition and diversification; (b) custodians and their activities; (c) information supplying requirements, including disclosure requirements for prospectuses and annual and semi-annual reports; and (d) limitations on borrowing and lending. In addition, managers must satisfy minimum capital requirements. They are also subject to limitations on non-investment management activities and delegation of responsibilities, and they must employ a risk management process which enables monitoring and measuring of the risk of positions and their contribution to the overall risk profile of the portfolio, have adequate internal controls and procedures and be structured in such a way as to minimize risks of conflicts of interest.

Classifying the IMMFs as other investments under Rule 3a-8(b)(8) would not reflect the spirit of Rule 3a-8. Rule 3a-8 was implemented to provide R&D Companies with the flexibility to invest in capital preservation instruments and other instruments that would fall within the definition of investment securities under Section 3(a)(2) without becoming subject to regulation under the Act.

Based on the objectives, portfolio, liquidity, ratings and regulation of the IMMFs, we believe that the IMMFs included in the Proposed Investments and Ark's Investment Policy would constitute capital preservation investments within the meaning of Rule 3a-8.

(b) **Certificates of Deposit**

Ark would like the ability to invest in CDs of financial institutions, including non-US financial institutions subject to regulation by a financial regulatory authority in one or more of the Permitted Member States, denominated in pounds, euros and/or dollars. A CD is issued by a financial institution and evidences a deposit made for a set period of time that provides a specific rate of interest. CDs are negotiable and, when traded on the secondary market, the price is determined by the term of the CD, the interest payable thereunder and the current market interest rate (the yield to maturity), and its nominal or face value. Again, Ark would like the ability to invest in CDs because their investment return is highly competitive compared to the returns offered by the Demand Deposits. As they are negotiable instruments with an active trading market, in addition to liquidity resulting from the limited term of the CD, the trading market also provides liquidity if funds are required prior to maturity.

Under the Investment Policy, Ark may only invest in CDs issued by financial institutions with a minimum short-term credit rating of P-1 by Moody's, A-1 by S&P or F1 by Fitch IBCA ("**Fitch**")³⁷ and, where applicable, a minimum long-term credit

³⁶ Within the EU, member states are required to adopt legislation in order to implement into their national laws the requirements of EU directives. Although national legislation and regulatory regimes differ, all are required to satisfy the minimum requirements set forth by the EU. With respect to UCITS, the relevant national legislation implements the Undertakings for Collective Investment in Transferable Securities Directive, 85/611/EC, as amended.

³⁷ For Moody's short-term bank deposit ratings, banks rated P-1 for deposits "offer superior credit quality and a very strong capacity for timely payment of short-term obligations". A rating of A-1 by S&P for short-term credit ratings means that the obligor "has a strong capacity to meet its financial commitments". Fitch International short-term credit

rating of at least A3 by Moody's, A- by S&P or A- by Fitch.³⁸ For those investments with a long-term credit rating only, the minimum rating must be at least Aa2 by Moody's, AA by S&P or AA by Fitch.³⁹ In addition, Ark may only invest in CDs that have a maximum maturity of 12 months or less. Any CDs issued by non-US financial institutions must be issued by established financial institutions in the EU that are regulated as to capital adequacy and other measures of financial soundness by a financial regulatory authority in one or more of the Permitted Member States. In addition, Ark's total exposure to any individual issuer in respect of all of the Permitted Investments may amount to no more than £10 million (or the equivalent in other currencies).

We note that ICOS Corporation adopted an investment policy that permitted it to invest in dollar and euro denominated CDs issued by non-US financial institutions,⁴⁰ and that Corvis Corporation adopted an investment policy that permitted it to invest in dollar denominated CDs issued by US financial institutions, but including foreign branches of US banks.⁴¹ The CDs that meet the requirements of Ark's Investment Policy should provide the required liquidity and limited credit risk in a manner similar to those CDs permitted by the investment policies submitted to the Commission in connection with the ICOS Order and the Corvis Order.

We further note that in the IBM Order⁴² granting IBM International Finance, N.V. and IBM International Treasury Services Company, *et al.* (together, "**IBM Finance**") an exemption from subparagraphs (a)(5) and (a)(6) and (b) of Rule 3a-5 under the Act ("**Rule 3a-5**") with respect to IBM Finance's proposed investment in certificates of deposit, time deposits and other money market instruments entered into with non-US banks, the Staff granted the relief sought on condition that "[a]ny time deposits, certificates of deposit, or similar money market instruments invested in by [IBM] Finance will have a maturity of no greater than six months⁴³ and will be entered into with established financial institutions in countries where such institutions are regulated as to their capital adequacy and other measures of financial soundness",⁴⁴ thus allowing IBM Finance to invest in these types of instruments although they are not included in the list of permitted

ratings deem F1 as the highest credit quality and "indicates the strongest capacity for timely payment of financial commitments".

³⁸ For Moody's long-term bank deposit ratings, banks rated A for deposits "offer good credit quality. However, elements may be present that suggest a susceptibility to impairment over the long term". A rating of A by S&P for long-term issuer credit ratings means the bank has a "strong capacity to meet its financial commitments but is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligors in higher-rated categories". Fitch International long-term credit ratings deem A as a high credit quality denoting a "low expectation of credit risk", which indicates that the "capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings".

³⁹ For Moody's long-term bank deposit ratings, banks rated Aa for deposits "offer excellent credit quality, but are rated lower than AAA banks because their susceptibility to long-term risks appears somewhat greater". A rating of AA by S&P for long-term credit ratings "differs from the highest-rated obligations only in a small degree" and means the bank has a "very strong capacity to meet its financial commitments". Fitch international long-term credit ratings deem AA as a very high credit quality denoting a "very low expectation of credit risk", which indicates a "very strong capacity for timely payment of financial commitments" that is "not significantly vulnerable to foreseeable events".

⁴⁰ See ICOS Investment Policy, *supra* note 29.

⁴¹ See Corvis Investment Policy, *supra* note 30.

⁴² IBM International Finance N.V., IBM International Treasury Services Company, et. al., Investment Company Act Release Nos. 19548 (June 29, 1993) (notice) (the "**IBM Notice**") and 19602 (July 28, 1993) (order granting exemption) (the "**IBM Order**").

⁴³ See the IBM Order, *id.*, (IBM Finance requested relief with respect to CDs and time deposits with a six months terms) and Hewlett-Packard Finance Company no-action letter (pub. avail. October 7, 1992) (the Staff granted no action relief to Hewlett-Packard Finance Company with respect to demand and time deposits with a maximum term of nine months) (the "**HPFC I No-Action Letter**").

⁴⁴ See IBM Notice, *supra* note 42, at C.3.

investments under Rule 3a-5 as long as they are short term and issued by a regulated non-US bank. Counsel to IBM Finance argued that "there is no investor protection concern based on the safety of the temporary investments requested".⁴⁵ The Staff allowed investments not originally included within the scope of Rule 3a-5(a)(6) where the investments are similar to other investments contemplated by Rule 3a-5 and not inconsistent with its purpose. By analogy, given the similar characteristics of permitted investments (*i.e.*, short term, low credit risk) under both Rule 3a-5 and Rule 3a-8, the CDs should be considered capital preservation investments under Rule 3a-8 as they are consistent with the purpose of Rule 3a-8 and pose low credit risk, are liquid and preserve capital.

As with the IMMFS, the non-US financial institutions issuing the CDs would be subject to regulation by a financial regulatory authority in one or more of the Permitted Member States. This regulation must, at a minimum, satisfy the requirements of EU directives.⁴⁶ These directives set forth requirements for: (a) initial and continued regulatory authorization; (b) capital adequacy, including separate capital adequacy requirements applicable to a bank's trading operations for its own account (unless minimal) and to the operations of other non-bank financial institutions; and (c) regulatory supervision, including over internal controls and procedures, solvency and risk management, and notification and approval of acquisitions of significant interests. In addition, an EU directive mandates that EU member states adopt deposit guarantee schemes that protect individual deposits up to an amount of at least €20,000 in the event that a bank becomes insolvent.⁴⁷ These schemes, however, are designed for the protection of small investors and, in the legislation adopted by the relevant EU member state in implementing this directive, companies of Ark's size may be excluded from the protection they offer. We note that under the US Federal Deposit Insurance Corporation, deposits are only guaranteed up to a maximum of \$100,000, and that neither the €20,000 nor \$100,000 levels would provide a meaningful level of protection for Ark's anticipated investments.

Given the characteristics of the CDs described above, we believe that the CDs included in the Proposed Investments and Ark's Investment Policy would constitute capital preservation investments within the meaning of Rule 3a-8.

(c) **Term Deposits**

Ark would also like the ability to invest in Term Deposits held with financial institutions, including non-US financial institutions subject to regulation by a financial regulatory authority in one or more of the Permitted Member States, denominated in pounds, euros and/or dollars. A Term Deposit is an interest-bearing deposit held with a financial institution that provides a specific rate of interest for a set period of time, typically for 30, 60 or 90 days, or for six or 12 months. A Term Deposit is non-negotiable and its interest rate is an annual rate payable over the term of the deposit. The interest rate and the yield to maturity are the same. Again, Ark would like the ability to invest in Term Deposits because

⁴⁵ IBM International Finance N.V., IBM International Treasury Services Company, et. al., Amended and Restated Application for an Order pursuant to Section 6(c) of the Investment Company Act of 1940 Granting an Exemption from the Provisions of Paragraphs (a)(5), (a)(6) and (b) of Rule 3a-5 under the Investment Company Act of 1940 (filed December 3, 1992), at page 20.

⁴⁶ See, e.g., Directive Relating to the Taking Up and Pursuit of the Business of Credit Institutions (2000/12/EC) (repealing and replacing, among other directives, First and Second Directives on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions (1977/780/EC and 1989/646/EC)), as amended; Directive on Investment Services in the Securities Field (1993/22/EC), as amended; and First and Second Directive on Capital Adequacy of Investment Firms and Credit Institutions (1993/6/EC and 1998/31/EC), as amended.

⁴⁷ See Directive on Deposit-Guarantee Schemes (1994/19/EC).

their investment return is highly competitive compared to the returns offered by the Demand Deposits.

Under the Investment Policy, Ark may only invest in Term Deposits held with financial institutions that have a minimum short-term credit rating of P-1 by Moody's, A-1 by S&P or F1 by Fitch⁴⁸ and, where applicable, a minimum long-term credit rating of at least A3 by Moody's, A- by S&P or A- by Fitch. For those investments with a long-term credit rating only, the minimum rating must be at least Aa2 by Moody's, AA by S&P or AA by Fitch.⁴⁹ Any Term Deposits held with non-US financial institutions must be held with established financial institutions in the EU that are regulated as to capital adequacy and other measures of financial soundness by a financial regulatory authority in one or more of the Permitted Member States. In addition, Ark's total exposure to any financial institution in respect of all of the Permitted Investments may amount to no more than £10 million (or the equivalent in other currencies).

Although the Term Deposits are not negotiable and thus may not be as liquid as the other Proposed Investments, in our view the Term Deposits would also qualify as capital preservation investments within the meaning of Rule 3a-8(b)(4). Under the Investment Policy, Ark may only invest in Term Deposits with a term of 12 months or less, and such investment would in any event be made with a view towards Ark's anticipated funding requirements. In declining to establish criteria for the definition of capital preservation investment in the Adopting Release, the Commission did not require that the capital preservation investments be negotiable and the Commission specifically stated that it would expect the "portfolio of an R&D company whose products require, on average, an additional eight years to develop to differ from the portfolio of another R&D company whose products are expected, on average, to be ready in two years, even though both companies would be investing with the goal of preserving capital and liquidity".⁵⁰ As discussed in paragraph 3.2 above, Ark does not expect any of its three lead products to reach the market before 2005. Accordingly, including in the Proposed Investments instruments such as the Term Deposits which cannot be traded but nevertheless have a maturity of 12 months or less is a reflection of the fact that Ark will not require immediate liquidity with respect to all of its financial resources. As set forth in the Investment Policy, Ark will maintain at all times a minimum of £2 million (or the equivalent in other currencies) of its financial resources payable on demand within 24 hours' notice (including any amounts held in Demand Deposits and IMMFs) to finance its immediate liquidity requirements.

We note that Corvis Corporation adopted an investment policy that permitted it to invest in dollar denominated Term Deposits with US financial institutions.⁵¹ The Term Deposits that meet the requirements of Ark's Investment Policy should provide the required liquidity and limited credit risk in a manner similar to those Term Deposits permitted by the investment policy submitted to the Commission in connection with the Corvis Order.

We further note that Term Deposits held by non-US banks were deemed permitted investments under Rule 3a-5(a)(6) in both the IBM Order and in the HPFC I No-Action Letter.⁵² In the HPFC I No-Action Letter, the Staff granted no-action relief to

⁴⁸ See description of short-term ratings, *supra* note 37.

⁴⁹ See description of long-term ratings, *supra* notes 38 and 39.

⁵⁰ See the Adopting Release, *supra* note 4, at footnote 29.

⁵¹ See the Corvis Investment Policy, *supra* note 30.

⁵² See the HPFC I No-Action Letter, *supra* note 43.

Hewlett-Packard Finance Company ("**HPFC**"), a finance subsidiary within the meaning of Rule 3a-5 of the Act, to invest in certain demand and time deposits with a maturity of less than nine months of various non-US banks ("**HPFC Deposits**") and certain repurchase agreements with respect to US Government securities, instruments not specifically listed as permitted investments in Rule 3a-5(a)(6). HPFC's counsel argued that the HPFC Deposits satisfy the intent of Rule 3a-5 because they had an overwhelming similarity to exempt Section 3(a)(3) commercial paper. In its response granting the no-action relief, the Staff stated that their position was based on "our belief that the [HPFC] Deposits and Repurchase Agreements are the types of short-term investments contemplated in Rule 3a-5 and, therefore HPFC's investments in these instruments would be consistent with the purposes of Rule 3a-5 . . .". As stated in subparagraph 4.3(b) above, by analogy, given the similar characteristics of permitted investments (*i.e.*, short term, low credit risk) under both Rule 3a-5 and Rule 3a-8, the Term Deposits should be considered capital preservation investments under Rule 3a-8 as they are consistent with the purpose of Rule 3a-8 and pose low credit risk, are liquid and preserve capital.

The non-US financial institutions with which the Term Deposits would be placed would be subject to the same type of regulatory oversight in one or more of the Permitted Member States as would apply to those institutions issuing the CDs.

Given the characteristics of the Term Deposits described above, we believe that the Term Deposits included in the Proposed Investments and Ark's Investment Policy would constitute capital preservation investments within the meaning of Rule 3a-8.

(d) **Commercial Paper**

Ark would also like the ability to invest in CP issued by financial institutions or corporate or government entities, including non-US institutions and entities, denominated in pounds, euros and/or dollars. Commercial paper is a short term unsecured promissory note of a financial institution or corporate or government entity with a term of 12 months or less. Commercial paper is negotiable and is generally traded on a discounted basis (*i.e.*, does not pay interest, but rather pays only principal at maturity) although may be interest-bearing instead. As they are negotiable instruments with an active trading market, in addition to liquidity resulting from the limited maturity of the CP, the trading market also provides liquidity if funds are required prior to maturity.

Under the Investment Policy, Ark may only invest in commercial paper with a short-term rating of P-1 by Moody's, A-1 by S&P and/or F1 by Fitch.⁵³ In addition, Ark's total exposure to any individual issuer in respect of all of the Permitted Investments may amount to no more than £10 million (or the equivalent in other currencies).

We note that ICOS Corporation adopted an investment policy that permitted it to invest in both US and non-US CP,⁵⁴ and that and that Corvis Corporation adopted an investment policy that permitted it to invest in US CP.⁵⁵ The CP that meets the requirements of Ark's Investment Policy should provide the required liquidity and limited credit risk in a manner similar to the CP permitted by the investment policies submitted to the Commission in connection with the ICOS Order and the Corvis Order.

⁵³ See description of short-term ratings, *supra* note 37. Each of the three ratings by the rating agencies is the highest in its category.

⁵⁴ See the ICOS Investment Policy, *supra* note 29

⁵⁵ See the Corvis Investment Policy, *supra* note 30.

Given the characteristics of the CP described above, we believe that the CP included in the Proposed Investments and Ark's Investment Policy would constitute capital preservation investments within the meaning of Rule 3a-8.

(e) **Government Securities**

Ark would also like the ability to invest in US government securities⁵⁶ and UK government securities, including conventional and index-linked gilts ("**Gilts**") and treasury bills ("**Treasury Bills**"). A Gilt is a UK government liability, denominated in pounds, issued by the UK Debt Management Office (the "**DMO**"), an executive agency of HM Treasury. Conventional and index-linked Gilts bear interest for a set period of time, typically five, ten or 30 years, at a rate that is either fixed or linked to the UK retail price index, respectively.⁵⁷ Treasury bills are short-term debt instruments with maturities of up to one year, although to date the DMO has only issued treasury bills with maturities of one, three or six months. Treasury bills are issued and traded on a discounted basis (they do not pay interest, but rather pay only principal at maturity). Gilts and Treasury Bills are negotiable and listed on the London Stock Exchange and, when traded on the secondary market, the price is determined by the term of the security, the interest payable thereunder and the current market interest rate (the yield to maturity), and the nominal or face value of the security.

The UK government bond market operates with a primary dealer system. As of December 31, 2003, there were 16 firms recognized by the DMO as Gilt-edged market makers ("**GEMMs**"), 11 of which were also recognized as index-linked GEMMs. Each GEMM must be a member of a recognized investment exchange (in practice, the London Stock Exchange) and must undertake a number of market-making obligations, including making effective two-way prices to customers on demand in all market conditions to provide liquidity for customers wishing to trade. In addition, as of December 31, 2003 there were nine primary participants for Treasury Bills that have agreed to provide secondary dealing levels for Treasury Bills.

As of December 31, 2003, the nominal value of outstanding Gilts amounted to £311.3 billion and the nominal value of outstanding Treasury Bills amounted to £24.0 billion.⁵⁸ The UK Gilts market comprises approximately 5% of international government bond indices and average daily trading volume in the Gilts market is approximately £11.0 billion.⁵⁹ As the Gilts and Treasury Bills are negotiable instruments with an active trading market, this provides liquidity if funds are required prior to maturity.

The Gilts and Treasury Bills are obligations of the UK government, which has been assigned the highest credit rating by all major rating agencies and has never failed to make interest or principal payments on Gilts as they fall due.

⁵⁶ Ark would invest in US government securities that fall within the definition of Government security contained in Section 2(a)(16) of the Act that, although not considered investment securities for purposes of Section 3(a)(1)(C) of the Act, would constitute investments in securities for purposes of Rule 3a-8(b)(7). We note that both the ICOS Investment Policy and the Corvis Investment Policy permitted investments in US government securities.

⁵⁷ In the past, the UK government has also issued "double-dated" Gilts with two maturity dates, which provide for a higher rate of interest after the first maturity date and allow for redemption by the UK government at any from the first maturity date until the final maturity date, and undated Gilts with no stated maturity date. The UK government has not issued these types of Gilts for a number of years and Ark does not intend to invest in these types of securities.

⁵⁸ UK Government Securities: a Guide to 'Gilts', UK Debt Management Office (February 16, 2004), at page 5 (avail. at www.dmo.gov.uk).

⁵⁹ *Id.*, at page 3.

We believe that the Gilts and Treasury Bills would qualify as capital preservation investments within the meaning of Rule 3a-8(b)(4) as they are obligations of the UK government, and thus of the highest credit rating, and have a highly liquid trading market. In addition, under the Investment Policy any Gilts and Treasury Bills would be required to have a remaining maturity of 12 months or less, so in addition to an active trading market the limited duration would also help to ensure and maintain liquidity. We note that US Government obligations are not characterized as investment securities for purposes of the 40% asset test under Section 3(a)(1)(C) of the Act. It would be against the intent of Rule 3a-8 if the Gilts and Treasury Bills, which share many of the features of US government obligations that serve protect investors, such as high credit quality and liquidity, were not treated as capital preservation investments. Classifying the Gilts and Treasury Bills as other investments under Rule 3a-8(b)(8) would not reflect the spirit of Rule 3a-8, which was implemented to provide R&D Companies with the flexibility to invest in capital preservation instruments and other instruments that would fall within the definition of investment securities under Section 3(a)(2) without becoming subject to regulation under the Act.

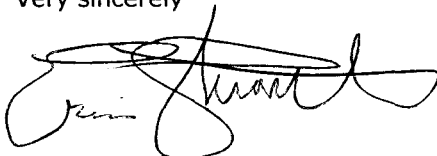
Given the characteristics of the Gilts and Treasury Bills described above, we believe that the Gilts and Treasury Bills included in the Proposed Investments and Ark's Investment Policy would constitute capital preservation investments within the meaning of Rule 3a-8.

5. **CONCLUSION**

Based on the foregoing, we request your concurrence that the Proposed Investments are capital preservation investments within the meaning of Rule 3a-8 of the Act.

If you have any questions or require any further information with respect to this request, please do not hesitate to call Marie Elena Angulo, Britta Jacobson or the undersigned on 011 44 20 7638 1111.

Very sincerely



Eric Stuart

Cc: Nigel Parker
Martyn Williams
David Ellam
Nick Plummer
(Ark Therapeutics Group plc)

Mark Lubbock
Anthony Clare
Daniel Bushner
Marie Elena Angulo
Britta Jacobson
(Ashurst)

ashurst

SCHEDULE A

ARK THERAPEUTICS GROUP PLC

INVESTMENT POLICY

This investment policy (this "**Policy**") has been adopted by resolution of the Board of Directors (the "**Board**") of Ark Therapeutics Group plc (the "**Company**") on 27th July 2004 with respect to the Company's investment portfolio (the "**Portfolio**") in order to conserve capital and maintain liquidity until the Company's funds (the "**Funds**") are used in its primary business. This Policy sets forth the eligible investments ("**Investments**") and the investment limits applicable to the Portfolio. The Portfolio is the responsibility of the Chief Financial Officer (the "**CFO**"). The CFO shall comply with this Policy in all actions taken with respect to the Portfolio.

1. **PURPOSE**

- 1.1 The Company's surplus Funds are held to meet the Company's working capital and fixed capital requirements. Funds are not held for the purpose of investment and at no time should the capital value of the Funds be put at unnecessary risk.

2. **INVESTMENT OBJECTIVES**

- 2.1 The objectives of the Portfolio are as follows:

- (a) to conserve capital;
- (b) to maintain sufficient liquidity to meet forecasted cash needs;
- (c) to maintain a diversified portfolio in order to minimise credit risk;
- (d) to keep surplus Funds fully invested, subject to this Policy; and
- (e) to maximise the Portfolio yield, subject to this Policy.

- 2.2 In addition, the Company must qualify for (and continue to qualify for) the exemption from registration as an investment company contained in Rule 3a-8 under the US Investment Company Act of 1940 .

3. **AUTHORISED INVESTMENTS**

3.1 **Investment Products**

The Portfolio may only contain the following Investments:

(a) **Term Deposits ("Term Deposits")**

A Term Deposit is an interest-bearing deposit that provides a specific rate of interest for a set period of time. A Term Deposit is non-negotiable. The interest rate is an annual rate payable over the term (the number of days) of the deposit. The interest rate and the yield to maturity are the same.

(b) **Certificate of Deposit ("CD")**

A CD is issued by a financial institution evidencing a deposit made for a set period of time that provides a specific rate of interest (the coupon). CD's are negotiable. When traded on the secondary market, the price is determined by the set period of time the CD was issued for, the coupon, the current market interest rate (the yield to maturity), the remaining life of the CD and the nominal or face value of the CD.

(c) **Commercial Paper ("CP")**

CP is an unsecured promissory note of a financial institution or corporate or government entity. CP is negotiable. CP is traded on a discounted basis (CP does not pay interest, but rather pays only principal at maturity).

(d) **International Money Market Funds ("IMMFs")**

IMMFs invest in short-term high quality debt instruments and provide the benefit of pooled investments, allowing investors to participate in a more diverse portfolio than they could on an individual basis. The assets are actively managed within very specific guidelines to offer safety of principal, liquidity and competitive returns.

(e) **US Government Obligations ("US Government Securities")**

US Government Securities are securities issued or guaranteed as to principal or interest by the United States (or a person controlled or supervised by and acting as an instrumentality of the US government) or any certificate of deposit of any of the foregoing, including treasury notes, bills and bonds issued by the United States or US federal agencies.

(f) **UK Government Obligations ("Gilts" and "Treasury Bills")**

A Gilt is a UK government liability, denominated in pounds sterling. Conventional and index-linked Gilts bear interest for a set period of time (typically five, ten or 30 years) at a rate that is either fixed or linked to the UK retail price index, respectively. Treasury bills are short-term debt instruments with maturities of up to one year issued and traded on a discounted basis. Gilts and Treasury Bills are negotiable. When traded on the secondary market, the price is determined by the term of the security, the interest payable thereunder and the current market interest rate (the yield to maturity), and the nominal or face value of the security.

3.2 **Investment Limits**

(a) **Credit Ratings**

All Investments must have an explicit rating by Moody's, Standard & Poor's and/or Fitch. For those Investments with a short-term credit rating, the minimum rating must be as follows: P1 (by Moody's), A1 (by Standard & Poor's) and/or F1 (by Fitch) and, where applicable, the minimum long-term credit rating must be as follows: A3 (by Moody's), A- (by Standard & Poor's) and/or A- (by Fitch). For those investments with a long-term credit rating only, the minimum rating must be as follows: Aa2 (by Moody's), AA (by Standard & Poor's) and/or AA (by Fitch).

(b) **Exposure Limits**

The total exposure to each of Barclays Bank plc ("**Barclays**"), Halifax Bank of Scotland plc ("**Halifax**"), and Royal Bank of Scotland plc ("**RBS**") taking into account any current balances, must not exceed £25 million (or the equivalent in other currencies). The total exposure to Barclays, Halifax or RBS, not taking into account any current balances held in the form of demand deposits, must not exceed £10 million (or the equivalent in other currencies). The total exposure to any other entity must not exceed £10 million (or the equivalent in other currencies). These total exposure limits shall be reviewed by the Board periodically in light of the amount of the Company's total Funds.

(c) **Maturity Profile**

All Investments must have a maximum maturity of 12 months or less. The maximum weighted average maturity of the Portfolio must not exceed 180 days. At all times a minimum of 20 per cent. of the Portfolio must have a maximum weighted average maturity of 90 days. At all times a minimum of £2 million must be payable on demand within 24 hours (including any current account balances and other demand deposits, and amounts invested in IMMFs).

(d) **Additional Restrictions on Term Deposits and CDs**

All Term Deposits and CDs held with or issued by non-US financial institutions must be held with or issued by established financial institutions regulated as to capital adequacy and other measures of financial soundness by a financial regulatory authority in one or more of the following countries: Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Spain, Sweden or the United Kingdom (the "**Permitted Member States**").

(e) **Additional Limits for IMMFs**

IMMFs must: (1) have a stated aim to protect capital and preserve liquidity; (2) have a money market fund rating of at least Aa by Moody's or AA by Standard & Poor's; (3) have no more than 5 per cent. of its assets invested with any one financial institution or corporate issuer; (4) have a weighted average maturity of 75 days or less; (5) have a stable or accumulating net asset value per share; (6) provide for same-day or next-day settlement upon redemption; (7) have minimum assets under management of £250 million (or the equivalent in other currencies); (8) be registered as an undertaking for collective investments in traded securities under relevant European Union directives and Permitted Member State legislation (9) be authorised by a financial regulatory authority in one or more of the Permitted Member States; and (10) have an investment manager authorised and regulated by a financial regulatory authority in one or more of the Permitted Member States.

4. **OPERATING PROCEDURES**

- 4.1 Identification of excess Funds available for investing and the investment of those Funds in accordance with this Policy are the responsibility of the CFO. The CFO may be assisted by the Company's Group Controller and external specialists. To help maximise the Portfolio yield within the limits applicable to the Portfolio set forth in this Policy, the CFO will, from time to time, use the services and resources of an international money brokers to obtain impartial and independent money market information. Such broker will be regulated by the UK Financial Services Authority (the "**FSA**") and bound by its code of conduct. The broker will act purely as an agent and not as a principal as laid out in the FSA regulations.
- 4.2 The transfer of Funds shall be made in accordance with the Barclays Bank mandate as approved by the Board of Directors.
- 4.3 The Audit/Investment Committee is responsible for reviewing the Portfolio for its compliance with this Policy on an annual basis. The Audit/Investment Committee is comprised of David Prince (Chairman), Sir Mark Richmond and Dr Wolfgang Plischke.

The Board of Directors is responsible for reviewing this Policy from time to time in order to assure its appropriateness.