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CONFLICT OF INTEREST PROBLEMS IN SBIC's

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HEARING
BEFORE A
SUBCOMMITTEE OF THE
COMMITTEE ON BANKING AND CURRENCY
UNITED STATES SENATE
EIGHTY-EIGHTH CONGRESS

FIRST SESSION

ON

S. 298

A BILL TO AMEND THE SMALL BUSINESS INVESTMENT ACT OF 1958

SEPTEMBER 5, 1963

Printed for the use of the
Committee on Banking and Currency

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CONFLICT OF INTEREST PROBLEMS IN SBIC'S

THURSDAY, SEPTEMBER 5, 1963

U.S. SENATE,
COMMITTEE ON BANKING AND CURRENCY,
SUBCOMMITTEE ON SMALL BUSINESS,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10:07 a.m., Senator William Proxmire, chairman of the subcommittee, presiding.

Present: Senators Proxmire (presiding), Dominick, and McIntyre. Senator PROXMIRE. Today the Small Business Subcommittee will receive testimony from representatives of SBA, SEC, and NASBIC regarding conflict of interest in the SBIC program.

This question received nationwide attention when, on July 2, 1963, the Wall Street Journal carried as its lead article a report entitled "Usual Federal Frown on Conflicts of Interest Absent in SBIC Cases." The article was very critical of SBA's handling of certain loans made by some SBIC's.

In considering small business legislation, the Small Business Subcommittee decided to hold additional hearings in order to gain a better understanding of this problem as it relates to SBIC's.

We have invited Mr. Foley, the new Administrator of SBA; Commissioner Whitney of the SEC, since the SEC has self-dealing problems with the investment companies under its jurisdiction; and Mr. Howard, president of NASBIC, to give us their views on this important question.

Without objection the Wall Street Journal article, my letter to SBA and Mr. Horne's reply, together with SBA regulations on self-dealing and a copy of the bill, S. 298, will be made part of the record of the hearings.

(The documents follow:)

[From the Wall Street Journal, July 2, 1963]

DOUBLE STANDARD—USUAL FEDERAL FROWN ON CONFLICTS OF INTEREST ABSENT IN SBIC CASES—SBA APPROVES MANY LOANS BY INVESTMENT GROUPS TO OFFICERS' OWN COMPANIES—WHERE SOME TAX DOLLARS GO

[A Wall Street Journal news roundup]

When the Government discovers what look like conflict-of-interest practices, it usually tries to stamp them out. But one adventurous Federal agency, the Small Business Administration, is taking a liberal tack: Officially, though in a shroud of secrecy, it is sponsoring intricate and interesting business arrangements which it designates as "self-dealing."

The Small Business Administration pours taxpayer money into hundreds of small business investment companies (SBIC's) scattered around the Nation, and these in turn mix it with private funds and lend to little businesses. In many instances the agency is formally authorizing these SBIC's to grant loans to enterprises in which SBIC officers themselves have a personal stake. The

phrase "self-dealing" refers to such interlocking intimacy between those who grant the money and those who get it.

Here's one sample of these perfectly legal arrangements:

James C. Nichols is vice president and secretary of Coast Small Business Investment Co., Pacific Grove, Calif. He put \$50,000 into this SBIC, as did each of two other owners. The Small Business Administration put in \$150,000, and guaranteed another \$150,000 in funds obtained from a bank.

Mr. Nichols is also sole owner of Nichols Plumbing & Heating Co. in Monterey, Calif. This year he wanted to buy a new building for his plumbing firm, but says he found "banks aren't too free with their money." He turned to the SBIC and received \$75,000, for 10 years, on terms which Coast SBIC Executive Secretary Robert W. Tuttle reports were more favorable than banks were willing to grant.

SURPRISED AT APPROVAL

"Obviously the loan wasn't made at arm's-length," remarks Mr. Tuttle, though he and the two other SBIC owners thoroughly examined its soundness. "Frankly, I was not optimistic," he recalls, about getting the deal approved by Small Business Administration headquarters in Washington. He was surprised when the agency quickly OK'd it, with an exchange of letters. But like others who are fostering such arrangements, he does consider them beneficial. "If the transaction is the kind you would have made with a stranger, then why not go ahead with your own people?"

Typically, SBIC officers, when seeking SBIC loans to ventures in which they have a personal stake, absent themselves from SBIC board meetings when their requests are being considered.

A majority of the Nation's 600-plus SBIC's apparently still avoid self-dealing. But in Washington, the boss of the Small Business Administration (SBA), John Horne, heartily contends the practice is desirable, to give SBIC officials "flexibility" in investment. Deputy Administrator James Parris, who signs the letters authorizing specific SBIC self-deals, adds: "Our main concern is securing capital for small businesses. We don't want to bog small SBIC's down with too many regulations."

This view contrasts with the proclaimed attitude of other Federal agencies, notably the Securities and Exchange Commission. Though all SBIC's come under Small Business Administration jurisdiction, those selling shares to the general public are further scrutinized by the SEC—and its officials declare most such SBIC's have "quit asking us to approve self-dealing because they know we won't." Privately, those SEC officials contend standards should be just as rigorous for SBIC's that escape SEC rules. Without discussing actual cases, they maintain that self-dealing SBIC officers could influence lending to their own failing enterprises—or get a "free ride" for their own investments in ventures made profitable by the injection of SBIC money.

CHALLENGING SELF-DEALING

"It is not necessary to prove actual damage" to the lending company "or even actual profit to (an) individual" to challenge self-dealing, SEC lawyers contended in a recent court case. "It is sufficient that the transaction be fraught with the possibility that the company might be injured by action based upon something less than disinterested motives on the part of its fiduciaries."

Of course, no sinister motive, need be implied by any loan application to an SBIC. The purpose of creating these lending institutions and giving them governmental financial support is to make money available to small businesses when they can't get it from banks—or at least can't get it for so long a repayment period, or for so low interest charges. This can be motive enough, either for arm's-length borrowing or for self-dealing borrowing.

When the SEC does get requests for approval of self-dealing arrangements, it makes them public. The Small Business Administration reveals no details of self-deals submitted or approved: Mr. Horne says his lawyers advise it should not. According to its officials, self-dealing has been permitted by SBA ever since Congress created the SBIC program 5 years ago, and nobody knows how many such transactions have occurred. Only last October the staff began keeping a current count, and by May discovered they had approved 33 self-dealing applications—at the rate of about 1 a week—while rejecting just 3.

Pressed by Wall Street Journal reporters, the Small Business Administration did reveal the names of these 36 SBIC's—while refusing to state even how

much taxpayer money has been handed to any of them. Deputy Administrator Parris quickly sent to each of these involved SBIC's a letter warning they might "receive inquiries" from the press and emphasizing that SBA, for its part, is keeping mum.

"It is not the present intention of SBA to release any information regarding the details of the specific transactions," he wrote. "We do not plan to provide information about the name or financial affairs" of those who got the self-dealing loans. "Nor do we plan to provide any explanation of how our general criteria in such matters were applied to specific cases. * * * Should you receive an inquiry on this subject the decision as to whether or not you release additional information rests entirely within your discretion."

Not surprisingly, many of the self-dealing SBIC's decided their "discretion" should take the form of telling reporters little or nothing.

"Ethical" considerations were cited by Benjamin Burdick, president of Midwest Small Business Investment Co., which shares quarters in Detroit with his law firm of Burdick, Burdick, Silverstein, & Burdick, and which has no fulltime employees. He declared Midwest has engaged in two self-dealing affairs, one of them very minor and both entirely legitimate, but said revealing details about borrowers could result in "crippling companies that ought not to be hurt."

"I'd rather not discuss it because I've read some of the Wall Street Journal articles about small business investment companies and they've been uncomplimentary," said A. B. Simms, president of both the First Atlanta Investment Corp. and the Southern Regional Association of Small Business Investment Companies. His own SBIC has the same address and phone number as an Atlanta real estate consulting firm, A. B. Simms & Associates.

"NO PHONEY-BALONEY"

G. Wayne Leslie, general manager of Judson-Murphy Capital Corp. in San Francisco, reported this SBIC made one self-dealing loan with "provisions so there was no phoney-baloney." He warmly defended "internally generated situations" as "the natural result of a small company; we haven't got the money to justify the cost of finders"—but said "we have a policy not to divulge information on any of our loans." Somewhat mystifyingly, the firm's president, Philip Murphy, insisted in a separate interview that this SBIC has made no self-dealing loans whatever, though it did seek an SBA opinion on what at first seemed a borderline case.

Greater Pittsburgh Capital Corp. has a distinguished board of directors including two vice presidents of Aluminum Co. of America. Its president, Wallace Kirkpatrick, an Allegheny Ludlum Steel Corp. executive, suggested there are "probably a lot of shady goings-on" among some other SBIC's, but said his own did better by engaging in two self-deals than it could have done lending to others. Nevertheless, no details were given out. Vice President Donald Collins explained details of deals are simply private and confidential matters, and besides, information about self-dealings by SBIC's can be "bad publicity" for the industry.

But spokesmen for a number of SBIC's appear glad to disclose such dealings, and laud their benefits.

Charles M. Fairchild, who deals in real estate and other ventures in Washington, D.C., is proud of his role in Citizens Small Business Corp. It was founded 3 years ago, and he joined some 40 other stockholders to provide a total of \$150,000 in private funds, while the Small Business Administration provided an equal amount of Government money. Mr. Fairchild became one of the nine directors; his wholly owned investment counseling concern, Fairchild & Co., was granted a contract to manage this SBIC. By now, Citizens has put \$106,000 of loans, more than a third of its capital, into two companies in which Mr. Fairchild has himself become an investor.

Recounting this, James Olah, an official of Fairchild & Co., gives further detail: Last year Citizens loaned \$60,000 to Branch Mountain Timber Farms, Inc., near Moorefield, W. Va. Before long, Mr. Fairchild had personally bought one-third ownership of the lumber company. By December, Citizens had granted another loan, of \$10,000.

LOANS TO ART FIRM

Two years ago Citizens had put \$30,000 into American Society of Fine Arts, Inc., while Mr. Fairchild was investing \$5,000 of his own in this firm set up to market art replicas. Last October Mr. Fairchild became president of the art company; in January it received another \$6,000 loan from Citizens.

In all its investment program, Citizens has granted second-helping loans only to these two companies.

Comments Mr. Fairchild: "Branch Mountain would be bankrupt right now if I hadn't personally gone in; Citizens would have lost money." As for American Society, he says, "it original management tried a direct mail advertising approach that didn't work, so I was made president; but then the company ran into legal problems with its franchisers and has not been able to get any merchandise to sell. This is undergoing arbitration now; if we win, we'll make money."

The Small Business Administration has put another \$150,000 of Federal funds into Capital Investors Corp. of Montana, an SBIC formed last fall in Missoula, Mont., by 15 businessmen, each of whom invested \$10,000. Among these was Keith Wright, who serves as director. With approval of SBA headquarters in Washington, Capital Investors made a \$26,000 10-year loan to Wright Lumber Co., in which Mr. Wright then held a minority share of ownership.

The money, along with a bank loan and additional personal investment by Mr. Wright, went to buy out two of his partners, to put Mr. Wright in full control of the lumber company, and to finance its expansion—so report high officials of the lending institutions concerned. Mr. Wright himself, despite a red and yellow "Welcome" sign outside his lumber company, says he's too busy to "waste time" talking to reporters.

MONTANA CARS, INC.

Another director of Capital Investors is Leonard Senechal, who holds a 40 percent stock interest in Montana Cars, Inc. This auto leasing firm has received a loan of about \$15,000 from the SBIC. "With 15 guys in business, at one time or another they are going to need money. It's natural to go where they have an investment," he remarks. Like Mr. Wright, he absented himself from the SBIC board meeting that approved his loan.

When Mr. Senechal helped found the SBIC, half his \$10,000 share was actually money advanced by Mills Folsom, past president of the Missoula Chamber of Commerce. The SBIC subsequently granted a \$20,000 loan for buying irrigating equipment to Folsom Co., Inc., a ranching enterprise owned by Mr. Folsom.

More recently, Mr. Folsom says, he found he needed to get back his original indirect investment in the SBIC. Since the SBIC could not immediately buy back these shares without impairing its required capital, the problem was solved by a further SBIC loan to Mr. Folsom of \$5,200 (his original investment plus interest); meanwhile his shares, nominally owned by Mr. Senechal, are in escrow. Says Mr. Folsom: "As far as I'm concerned, the stock is gone."

Some SBIC's, after gaining formal approval from Washington for particular self-deals, have been overwhelmed by doubts.

"COLD FEET"

"We got cold feet," says Gerado Joffe, president of Science Investment Co. in San Francisco. This year the Small Business Administration had okayed the SBIC's plan to back a company formed to produce Tar Gard, a do-it-yourself cigarette filter which smokers could fit on the tips of regular brands. Mr. Joffe and Forrest Tancer, vice president of the SBIC, each personally owned 25 percent of Tar Gard Corp. After brooding, they decided to drop the SBIC deal and obtain their filter money elsewhere. Says Mr. Joffe: "If anything went wrong with the loan it would have been very unpleasant for us" with the other 21 SBIC stockholders.

Differing views about self-dealing are illustrated by Robert M. Nason, president of Arizona Capital Corp., in Tucson. One director of this SBIC insisted he did not want to borrow from it and obtained money elsewhere. But SBA approval has been sought and granted for a \$60,000 loan to a company in which another director, F. C. Thum, holds an interest. Mr. Thum is president of this concern, John Porter Manufacturing Co., of Phoenix; the SBA letter of approval noted he owns less than 5 percent of its stock but holds an option which would give him 31-percent equity.

SBA officials say they apply three criteria to self-dealing applications. First, there must be noninterested persons in the SBIC with power to block the transaction if they wanted to. Second, terms of the deal must be "fair and reasonable." Third, the arrangement must "serve the purposes of the Small Business Investment Act of 1958." Though this may seem vague, and though officials refuse to elaborate, it has been used to reject a few proposals.

Neil Christopher, president of Southern Small Business Investment Co., in New Orleans, says Washington prohibited a \$86,000 loan intended for Hammond Homes, a real estate development firm. SBA objected that Southern SBIC was controlled by a mortgage company in which Mr. Christopher and an associate together held 49.5-percent ownership; that the two of them owned all of Hammond Homes; that the projected deal "would constitute a use of the (SBIC) by its owners as a financing medium of their own undertaking."

Complains Mr. Christopher: "If the SBA was justified in turning down this loan, it should have turned down a lot of the others it has approved. I think a lot of SBIC's have gotten loans that were the same kind as mine. It might be that some of the others didn't furnish full information."

SBA OPERATIONS

How much information the SBA does demand remains obscure. Its officials say they do not normally attempt on scene investigations before approving self-deals, though traveling examiners may later look into them during routine checks made every year or two. Washington operates mainly by correspondence. And its letters of approval seen by reporters merely recite back to the self-dealing SBIC the same information the SBIC has provided. Sometimes Washington takes months to make up its mind. But SBA took only two days to clear a deal for Chicago Capital Corp.; a director of this SBIC happened to be partner in a law firm serving as legal counsel for a company which obtained a loan, and he also served as a director and secretary of his borrowing company—but he had no financial interest in it.

In some cases the Small Business Administration may be getting slightly less than the full story.

Gerald Hardwick, president of First West Texas Capital Corp., in Odessa, Tex., pulled out of the files for a visiting reporter a letter from SBA authorizing a loan "in the amount of \$62,500" to Rebel Pipe & Supply Co., Inc., partially owned by J. D. Ormand, a director of the SBIC. The loan actually granted was \$85,000, however, he declared. He explained that after filing its applications this SBIC had increased its capital surplus, which raised its ceiling on the size of any one loan—so he didn't think further approval by SBA was necessary.

"If it hadn't been a good loan, I would have voted 'no' myself," commented Mr. Ormand. He declined to disclose earnings of Rebel, a small oilfield equipment concern. According to the SBIC's annual report, however, Rebel showed a profit of \$13,960 at the end of its last fiscal year, August 31, 1962, and a loss of \$9,533 through February 28 of this year. The SBIC itself operated at a \$7,520 loss in the year ended March 31. It has received \$470,000 in taxpayer money from the SBA.

MANY REAL ESTATE VENTURES

Though SBIC's on the SBA's list of "self-dealers" enter diverse ventures, they appear to find a special magnetism in real estate. And with full approval of the Small Business Administration—although this agency, when operating under a separate direct-loan program to small businesses, proclaims that it will not back "speculation in any kind of real or personal property" because of its "unique responsibilities as a lender of taxpayers' money."

"Congress should have been more specific in the type of investments it allows the SBIC's to make. I don't think they should allow real estate loans; there is plenty of venture money available for real estate development." So says Ezra Mintz, portfolio manager for Georgia Capital Corp., of Atlanta. Nevertheless this SBIC, which has drawn \$600,000 in Federal funds, made two \$60,000 loans last year to a real estate holding company whose president at the time was a vice president of Georgia Capital, he reports. Details are withheld because they are of "a personal nature."

In the Boston area, all three of the SBIC's which SBA reports as having received approval for self-dealing share their offices with real estate firms, and their transactions have involved real estate in some form.

Alan Zuker, treasurer of Chestnut Hill Capital Corp., says that when this SBIC took a third mortgage on a Boston apartment house owned by Diwal Trust, it granted an interest rate of 10 percent, somewhat lower than for other borrowers. The reason, he reports, is that Chestnut Hill's president, Robert Waldman, is as a stockholder entitled to a special rate, and he is a trustee of Diwal Trust. Says Mr. Waldman: "There was sufficient equity in the property to merit the loan."

COLONY HOTEL CORP.

Julian Cohen, treasurer of Massapoag Investment Corp., in Brookline, Mass., and a partner in the real estate firm which shares office quarters, says that this SBIC's deal cleared by SBA did not really involve self-dealing. He states Massapoag granted a \$54,000 mortgage for his brother, Bernard Cohen, on the Colony Hotel Corp., in Swampscott.

Bernard Berkman is a man of many interests who likewise denies any real self-dealing. He says he sells insurance and owns a liquor store and operates—within one office in Brookline—a real estate firm, Berkman, Associates, Inc., and Pilgrim Capital Corp., an SBIC. He is president of both. Phillip Lemelman is clerk (secretary) and a director of the SBIC; his son, Herbert Lemelman, is clerk of Berkman Associates, according to Mr. Berkman; the Lemelmans have joint law offices.

Pilgrim loaned \$17,500 to Wendell Realty Corp. last year on a Boston guest house, subject to a previous bank mortgage, according to Mr. Berkman. Treasurer of Wendell Realty is Phillip Lemelman; he declines to comment on the deal but his son Herbert says, "my father is a substantial owner of Wendell."

Mr. Berkman declares SBA approval was also gained for \$30,000 second mortgage granted last September to Bayside Manor Nursing Home, Inc., of which Herbert Lemelman was an incorporator. Pilgrim also has granted Bayside short-term loans from time to time, Mr. Berkman says, "Pilgrim agreed to buy 50 shares of Bayside stock, but the price has not been determined as yet," adds Mr. Berkman. Bayside's president Richard Gens, states that Pilgrim has obtained the 50 shares, amounting to half ownership, paying nothing for his stock since it was granted in return for a "favorable" 3 percent interest rate on the loans. "They put in the venture capital and we put in the know-how," comments Mr. Gens.

Herbert Lemelman declines to confirm Mr. Berkman's statement that he or his father obtained SBA approval on behalf of Pilgrim for the Bayside and Wendell loans. "It is not a matter of public record," he comments. He insists neither he nor his father engaged in self-dealing. "We are lawyers and professional clerks and we do this all the time; we have no (investment) interest in Bayside or Pilgrim." Mr. Berkman states that he personally owns all of Pilgrim's stock, with \$154,000 of his own capital and \$150,000 borrowings from SBA. And he too insists none of Pilgrim's transactions constitute self-dealing.

Richard Felts, manager of Small Business Investment Corp. of Georgia, says it lent \$45,000 last summer to Pleasant Hill Acres, Inc., which wanted to develop a trailer park at the edge of Atlanta. Two of this SBIC's directors owned 20 percent shares in Pleasant Hill. Since the SBIC had previously invested in a trailer sales agency, explains Mr. Felts, "I looked upon the creation of this mobile home park as a potential to sell some of our trailers." He adds: "We're not deliberately going into self-dealing transactions; we'd rather avoid them. It's going to be hard, because each of our 27 directors has diverse business interests around town * * * we don't want to turn down a good deal."

When SBA Deputy Administrator Parris officially approved a \$60,000 loan to Crossroads Development, Inc., by Small Business Investment Co. of Hawaii, an SBIC in Honolulu, he wrote that "Crossroads is stated to be a real estate development company, with two projects currently underway and plans for continuing series of development projects." He noted, with his approval that, Crossroads was wholly owned by Robert D. Thomas, vice president of the SBIC. Mr. Thomas has invested \$5,000 in this SBIC, according to its officials, while the SBA has put in \$300,000.

JULY 2, 1963.

HON. JOHN HORNE,
*Office of the Administrator,
Small Business Administration,
Washington, D.C.*

DEAR JOHN: I call your attention to the lead article in the Tuesday, July 2, Wall Street Journal entitled, "Usual Federal Frown on Conflicts of Interest Absent in SBIC Cases," with the subheadline, "SBA Approves Many Loans by Investment Groups to Officers' Own Companies."

This article deeply concerned me. The explanation in the article of the SBA's position did not seem to be very convincing.

The article indicated that SBA officials said they applied three criteria in passing on self-dealing arrangements. These criteria were as follows:

1. There must be noninterested persons in SBIC's with power to block the transactions if they want to do so.
2. The terms of the deal must be fair and reasonable.
3. The arrangement must serve the purposes of the Small Business Investment Act of 1958.

Obviously, these criteria are so vague as to be virtually meaningless. You know as I do that so-called noninterested persons closely associated with their colleagues in an SBIC are very likely to be subject to the pressures, influences, and associations which would persuade them to go along with self-dealing arrangements.

The examples given in the article of self-dealing by SBIC's in real estate ventures and speculations were particularly alarming.

But what gives me the deepest concern about this situation is the refusal of the SBA to disclose to the press the full and complete story on self-dealing. It is obvious that this kind of activity can be subject to grave abuse.

This abuse is particularly likely, however, if the whole business is conducted in secrecy with the public shut out.

In view of the fact that taxpayer money is involved in all of these cases, it is very difficult for me to understand how the SBA not only permits but, on the basis of this article, seems to encourage this highly questionable activity.

I would appreciate a prompt answer because I feel very strongly that this is something that should be considered by our subcommittee when we review the annual authorizations requested for SBIC's.

Sincerely,

WILLIAM PROXMIRE, *U.S. Senator.*

SMALL BUSINESS ADMINISTRATION,
Washington, D.C., July 9, 1963.

Hon. WILLIAM PROXMIRE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR PROXMIRE: This is in reply to your letter of July 2, 1963, requesting our specific comments on the article of July 2, in the Wall Street Journal entitled, "Usual Federal Frown on Conflicts of Interest Absent in SBIC Cases."

We appreciate this opportunity to explain our position since the Wall Street Journal article contains a number of statements that are misleading, incomplete, or only partly true. This is not surprising since, from past experience, we know that the Wall Street Journal can hardly be regarded as an objective observer of small business problems of "Main Street."

The purpose of this letter, however, is not to answer all of the misleading points of the Journal article, but to answer the points raised by your letter. For convenience, we first will list the four basic points or implied questions set forth in your letter.

1. Does SBA "encourage this highly questionable activity" (i.e., transactions labeled for convenience as "self deals" but which would be better described as transactions involving affiliation of interest between an SBIC and a small business concern in which the SBIC invests)?

2. Are the three criteria used by SBA in reviewing such transactions "so vague as to be virtually meaningless"?

3. Should SBA have refused to "disclose to the press the full and complete story on self-dealing"?

4. Should the "examples given in the article of self-dealing by SBIC's in real estate ventures and speculations" be regarded as "particularly alarming"?

At the outset, it should be noted that "self-dealing" is regulated by SBA under section 107.716 of the regulations, which provides as follows:

"§ 107.716 self-dealing limitation.

"(a) Self-dealing to the prejudice of SBA or the Licensee's shareholders is prohibited.

"(b) Without the prior written approval of SBA, a Licensee shall not purchase Equity Securities of, or make a loan to, an officer or a director of the

Licensee, or any person owning or controlling, directly or indirectly ten or more percent of the stock of said Licensee, or any close relative of such officer, director, or stock owner or controller, nor shall the Licensee purchase Equity Securities of or make a loan to any company in which such officer or director or such owner or controller of the Licensee's stock, or his close relative is an officer or director or owns or controls ten or more percent of the stock of such company: *Provided, further*, That without the prior written approval of SBA a Licensee shall not make such purchase of such securities or make such loan within six months after the termination of such officership or directorship in the Licensee, or within six months after the termination of such ownership or control of ten or more percent of the Licensee's stock. Nothing herein contained is intended to preclude a Licensee from permitting an officer, employee or representative from serving as a director, officer, or in any other capacity in the management of a small business concern for the purpose of protecting its investment in or loan to such concern.

"(c) Without the prior written approval of SBA, no Licensee, nor any officer or director thereof, shall borrow money from a small business concern, or from any officer, director or owner thereof, which has sold Equity Securities as defined in § 107.501 to or has borrowed money from said Licensee."

In this connection, it should be noted that SBA's procedure and regulations in this respect have been in effect continuously since 1959.

1. Does SBA "encourage this highly questionable activity"?

The article states that SBA officials are "sponsoring" financial transactions that involve various degrees of affiliation between principals of an SBIC and a small business concern. In the first place, SBA does not "sponsor" any investment made by an SBIC. Each SBIC, as a privately owned and operated corporation, has complete authority and sole responsibility to determine which investments it will make, so long as such investments are permissible under the provisions of the Small Business Investment Act and the regulations.

In the second place, there is a distinct difference between granting an exception from the prohibition of a regulation and the "sponsoring" of a transaction. The kind of transaction discussed in the article is prohibited, except where prior SBA approval has been obtained.

Regarding the comment that "taxpayer money is involved" in these transactions, this program does not provide grants of Federal money but rather provides for Federal loans to SBIC's. Moreover, substantial private investment must be made before Federal funds are available. Even in transactions where there is some element of affiliated interest, the individual investments of the SBIC stockholders are at stake since their investments are subordinated to Federal funds.

It should be noted that many of the affiliated transactions approved by this Agency do not involve an affiliation created by substantial stock interest by the same person in both the SBIC and small business concern. The affiliation more often is created by a director or officer of the SBIC who is a director or officer of a small business concern. These transactions arise more frequently in the smaller SBIC's that are serving a particularly community, where many of the officers and directors are local small businessmen whose businesses need financial assistance. It is only natural that these men would turn to the SBIC with which they are associated. Analysis of the cases mentioned in the Journal will bear out our contention that this is primarily a problem of the smaller SBIC's. To recognize that this problem of small SBIC's exists and to regulate it is hardly the same as saying that we are "sponsoring" this kind of financial transaction.

During the 9-month period ended June 30, 1963, of 45 applications for SBA approval of an "affiliated interest" investment or loan, processed to completion, 38 were approved and 7 were denied. Of the 38 approved, only 3 involved companies having statutory capital and paid-in surplus in excess of \$1 million. The total investments made by the 38 companies that were granted approvals were approximately \$3 million. During the same 9-month period, the amount of long-term loans and equity capital invested by about 650 licenses was at the rate of about \$14 million per month, or approximately \$126 million.

2. *Are the three criteria used by SBA in reviewing such transactions "so vague as to be virtually meaningless"?*

On the surface, it would seem desirable to have detailed and very specific tests for reviewing transactions involving affiliated interests. A review, however, of statutes, regulations, and court decisions applicable to other regulated investment companies, banks, financial institutions, and fiduciary duties of corporate officers reveals that the tests used are generally broad in nature.

For example, under the Investment Company Act of 1940 (to which many SBIC's are subject), Congress itself used broad standards with respect to financial transactions between affiliated persons that might be permissible upon application. Thus, section 17(b) of the 1940 act provides that the Commission may exempt certain otherwise prohibited financial transactions between affiliated persons if the evidence establishes that "(1) the terms of the proposed transactions * * * are reasonable and fair and do not involve overreaching on the part of any person concerned, (2) the proposed transaction is consistent with the policy of each registered investment company concerned * * * and (3) the proposed transaction is consistent with the general purposes of this title [the 1940 act]." In addition, section 21(b) of the 1940 act prohibits with one exception so-called "upstream loans" (that is, loans by an investment company to any person that "controls" or is "under common control" with the investment company). These 1940 act tests are quite similar to the standards that are applied by SBA which are summarized in the Journal and in your letter.

3. *Should SBA have refused to "disclose to the press the full and complete story on self-dealing"?*

The purpose of the SBIC program is to assist small business concerns to obtain long-term funds on reasonable terms. In line with that purpose, we have reduced as much as possible, consistent with the protection of Government funds and of small business firms, the administrative burdens placed on SBIC's which they, in turn, would have to place on their small business clients. Also consistent with SBA's policy, established in 1953 under the Small Business Act, we have treated business data of small business concerns and SBIC's on a confidential basis under the Small Business Investment Act.

Furthermore, the Small Business Investment Act does not require SBA to act pursuant to order, after appropriate notice and opportunity for hearing, or to make public disclosure of information filed by SBIC's in this area. In contrast, the SEC is required by section 40 of the Investment Company Act to act by notice and other and by section 45 to make public disclosure of information filed with it, unless the SEC finds that public disclosure is "neither necessary nor appropriate in the public interest or for the protection of investors."

The statutory responsibility of this Agency has been to develop a good regulatory balance between protection of Government funds and small business concerns on the one hand and the establishment of a "program to stimulate and supplement the flow of private equity capital and long-term funds which small business concerns need for the sound financing of their business operations and for their growth * * *" (sec. 102 of the Small Business Investment Act). This dual responsibility was pointed out with considerable emphasis to the Journal at the time of its inquiry. Unfortunately, on this point the Journal merely noted: "our main concern is securing capital for small businesses. We don't want to bog small SBIC's down with too many regulations."

In the absence of a statutory obligation for administrative procedures of the type found in the 1940 act, and for the other administrative reasons cited above, SBA determined from the inception of the SBIC program not to have formal procedures but, nevertheless, to apply administratively tests similar to those of the 1940 act. We believe that this is the best way, on balance, of achieving the objectives of the Small Business Investment Act.

4. *Should the "examples given in the article of self-dealing by SBIC's in real estate ventures and speculations" be regarded as "particularly alarming"?*

Under section 107.715 of the regulations, there are certain categories of prohibited investments, including the following:

"(e) Financing land speculations of small business concerns: *Provided, however,* That small business concerns may use funds for the acquisition and prompt development of land.

"(f) Any corporation, individual, partnership, or any other entity that is not engaged in a business operation conducted as a regular and continuous activity. The mere ownership of property and the collection of rents, income, or profits therefrom shall not constitute a business operation. * * *"

Although these regulations (including the specific prohibition on "financing land speculations," cited above), were called to the attention of the Journal, the article made it appear that SBA was concerned only with prohibition of real estate speculation in its direct lending program. The above regulations represent current experience in this particular area, having been revised several times to take care of problems that have arisen. If, in the future, through further experience, we find that current regulations do not prevent undesirable practices in this area, you may be assured that we will develop additional regulations on this subject. Mindful that this is a young and dynamic program, we are constantly aware that revisions and additions to existing regulations may be required.

As to the merit of real estate investments per se, it is common knowledge that real estate development and construction is making a significant contribution to the economy and that it is a field occupied in major part by small business concerns. Thus, in the June 29 issue of Business Week, it was noted that "new support for the second half (of the year) seems to be coming (1) from construction generally and housing in particular and (2) rising outlays on plant and equipment." Also, economic reports show that in 1961, our national income was \$427.8 billion. Of this amount, \$49.9 billion originated in real estate and construction (\$27.7 billion in real estate and \$22.2 billion in construction.) In the first quarter of 1959, there were 301,604 contract construction business units reporting under the old age, survivors and disability insurance program. Of this number, 87,830 were general building contractors. All but 894 of these had fewer than 100 employees.

In view of this contribution and of the fact that such investments are not prohibited by the Small Business Investment Act, we do not deem it advisable, based upon the examples cited in the Journal article, to curtail precipitously, SBIC investments in the real estate and construction field; however, we do not want real estate transactions to become too large a part of the overall program, and we are presently studying the situation to determine whether or not in our opinion we need additional regulations on this subject.

In addition to the specific response to points enumerated above, we would like to make the following general comments.

Early in this reply, we indicated that the Journal's article was incorrect and misleading. The very caption of the article proves this point. It states, "Double Standard—Usual Federal Frown on Conflicts of Interest Absent in SBIC Cases." As shown above, the standards of SBA are similar to those of the SEC. Under both the Investment Act of 1940 and the regulations of SBA under the Small Business Investments Act, affiliated financial transactions are permitted only with specific agency approval.

The bias of the Journal is further shown by its statement in its editorial on July 8, that, "Though self-dealing is perfectly legal—and may even be profitable for the SBIC's—some Federal agencies fail to share the SBA's enthusiasm for it." At no time did any official of SBA state that we were enthusiastic about transactions involving affiliated interests. What we did state was that we believe our policy, regulations, and procedures with respect to such transactions are appropriate, taking into balance all the complex factors involved which we have discussed above.

We also advised the Journal that the changing conditions in this young program may require revision of agency regulations in this area. In that connection we noted that there was pending in Congress, a bill that would transfer sole regulatory power over SBIC's to the SBA (H.R. 2422). This bill includes the prohibitions of the Investment Company Act of 1940 with respect to affiliated transactions, including a flat prohibition on "upstream loans." This bill was called to the attention of the Journal.

We reported to the Journal (but it failed to note) that we estimated that the great majority of SBIC's (because of closely held stock distribution) would be subject to the highly prohibitive Federal income taxes applicable to personal holding companies in the event these SBIC's engaged in affiliated transactions

involving substantial cross ownership of stock between SBIC's and small business concerns. In addition to this group of SBIC's, there is a substantial number of other SBIC's that are subject to the Investment Company Act of 1940. Another substantial group consists of subsidiaries or affiliates of bank holding companies and banks whose parent companies are subject to bank examination and regulation. In short, the SBA review of such transactions is not the only procedure through which potential abuses may be prevented.

In addition to the possibility of providing for definite prohibitions in this area by H.R. 2422 referred to above, we recognize that as the SBIC program matures, it may be desirable to change our approach on disclosure in the direction of procedural formality. We stated to the Journal that this matter is now and will be a subject of continuing consideration. However, if a formal procedure requiring public notice and hearing on request of interested parties were required in connection with applications for approval of affiliated transactions, it might well lead to a requirement in such cases that SBA make full public disclosure of all of its files relating to such SBIC's and their portfolio small business companies. We are concerned that such a disclosure requirement might be detrimental to small business concerns. As our files are presently organized, there is much business data concerning small business concerns in the SBIC's portfolios that could be quite detrimental to the success of these portfolio companies if such data were subject to full disclosure and public inspection. This is particularly true in the case of a small SBIC of local orientation.

A similar attitude on the part of bankers and bank regulators as to the protection of customers' affairs, is noted in a recent article in the New York Times. In the Times article, published on July 4, 1963, page 21, under the caption, "Problem for Bankers—Dispute Exists on Disclosure of Those Who Give Views to Public Agencies," it was noted that the New York Banking Department, the Federal Controller of the Currency, the Federal Reserve Board, and the Federal Deposit Insurance Corporation were unanimously opposed to public disclosure of communications received from persons supporting or opposing branch, merger, and charter applications before bank regulatory bodies. One of the reasons given for such opposition was stated as follows: "* * * the bank opposing the application may support its argument with facts about its own business which inevitably tend to tell something about the business of its customers. *Bankers and bank regulators feel strongly that a bank's customers' affairs should not be revealed.*" [Emphasis supplied.]

As in the case of agencies supervising banks, we rely very heavily on the procedure of examination of companies. We believe that our examination techniques, which are similar to bank examinations, provide considerable protection against potential abuses in this area. Where these examinations have disclosed violations of regulations (including misrepresentation of facts in applications for agency exemptive approvals), we have required corrective action by the SBIC and in some cases, we have suggested that the SBIC should surrender its license, and the SBIC has done so.

As a result of our examination of one company, we were able to render significant support to the Department of Justice in the prosecution and conviction of an office manager of one licensed SBIC for the fraudulent manipulation of Government funds. In viewing the SBIC industry as a whole, however, we concur with the Senate Select Committee on Small Business that observed in its 1960 report that "men of a high type and of great vision and courage are, generally, in control of SBIC's."

It should be noted also that the implication in the Journal article that the SEC never grants approval for affiliated financial transactions is untrue. The annual reports of the SEC show that from fiscal year 1958 through fiscal year 1962, the SEC has processed and closed applications with respect to affiliated financial transactions pursuant to section 17 of the 1940 act, on all kinds of investment companies, at the average annual rate of about 28. Although these reports do not show the number of cases approved, we understand that practically all cases not withdrawn by the applicants were approved. On the 42

section 17 applications processed in fiscal year 1962 by the SEC, 4 of the applications approved by the SEC in that year were applications filed by SBIC's.

We believe that we have administered the Small Business Investment Act and the regulations in accordance with the broad statutory objectives set by Congress and in line with the need for giving necessary flexibility to private management of the SBIC's.

We, of course, always are ready and desirous of improving our operations so as to better carry out the purposes of the Small Business Investment Act. To that end, we will continue to cooperate fully with your subcommittee and other appropriate committees of the Congress.

With kind regards, I am,

Sincerely,

JOHN E. HORNE, *Administrator.*

[Excerpt from SBA Regulations]

§ 107.716 Self-dealing limitation.

(a) Self-dealing to the prejudice of SBA or the Licensee's shareholders is prohibited.

(b) Without the prior written approval of SBA, a Licensee shall not purchase Equity Securities of, or make a loan to, an officer or a director of the Licensee, or any person owning or controlling, directly or indirectly ten or more percent of the stock of said Licensee, or any close relative of such officer, director, or stock owner or controller, nor shall the Licensee purchase Equity Securities of or make a loan to any company in which such officer or director or such owner or controller of the Licensee's stock, or his close relative is an officer or director or owns or controls ten or more percent of the stock of such company: *Provided, further,* That without the prior written approval of SBA a Licensee shall not make such purchase of such securities or make such loan within six months after the termination of such officership or directorship in the Licensee, or within six months after the termination of such ownership or control of ten or more percent of the Licensee's stock. Nothing herein contained is intended to preclude a Licensee from permitting an officer, employee or representative from serving as a director, officer, or in any other capacity in the management of a small business concern for the purpose of protecting its investment in or loan to such concern.

(c) Without the prior written approval of SBA, no Licensee, nor any officer or director thereof, shall borrow money from a small business concern, or from any officer, director or owner thereof, which has sold Equity Securities as defined in § 107.501 to or has borrowed money from said Licensee.

88TH CONGRESS
1ST SESSION

S. 298

IN THE SENATE OF THE UNITED STATES

JANUARY 18 (legislative day, JANUARY 15), 1963

Mr. SPARKMAN (for himself, Mr. HUMPHREY, Mr. SMATHERS, Mr. MORSE, Mr. BIBLE, Mr. RANDOLPH, Mr. ENGLE, Mr. BARTLET, Mr. WILLIAMS of New Jersey, Mr. MOSS, Mr. SALTONSTALL, Mr. JAVITS, Mr. COOPER, Mr. SCOTT, Mr. PROUTY, and Mr. COTTON) introduced the following bill; which was read twice and referred to the Committee on Banking and Currency

A BILL

To amend the Small Business Investment Act of 1958.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That this Act may be cited as the "Small Business Invest-
4 ment Act Amendments of 1963".

5 SEC. 2. The second sentence of section 302 (a) of the
6 Small Business Investment Act of 1958 is amended by strik-
7 ing out "\$400,000" and inserting in lieu thereof "\$1,000,-
8 000" and by striking out "three years" and inserting in lieu
9 thereof "seven years".

★I

1 SEC. 3. Section 303 (b) of the Small Business Invest-
2 ment Act of 1958 is amended to read as follows:

3 “(b) To encourage the formation and growth of small
4 business investment companies, the Administration is
5 authorized (but only to the extent that the necessary funds
6 are not available to the company involved from private
7 sources on reasonable terms) to lend funds to such companies
8 either directly or by loans made or effected in cooperation
9 with banks or other lending institutions through agreements
10 to participate on an immediate or deferred (standby) basis.
11 Such loans shall bear interest at such rate and contain such
12 other terms as the Administration may fix, and shall be
13 subject to the following restrictions and limitations:

14 “(1) The total amount of the Administration's share of
15 loans made and outstanding under this subsection (b) to any
16 one company at any one time (including direct loans, the
17 Administration's share of loans made hereunder pursuant to
18 agreements to participate on an immediate basis, and com-
19 mitments to lend directly or on an immediate participation
20 basis, but excluding loans made hereunder pursuant to agree-
21 ments to participate on a deferred (standby) basis and any
22 obligations acquired pursuant to such deferred participation
23 (standby) agreements) shall not exceed an amount equal to
24 50 per centum of the paid-in capital and surplus of such com-
25 pany or \$4,000,000, whichever is less. The total amount of

3

1 the Administration's share of all loans made and outstanding
2 under this subsection (b) to any one company at any one
3 time, including loans made hereunder pursuant to agreements
4 to participate on a deferred (standby) basis and any obliga-
5 tions acquired pursuant to such deferred participation
6 (standby) agreements, shall not exceed an amount equal to
7 the paid-in capital and surplus of such company or
8 \$8,000,000, whichever is less.

9 " (2) All loans made under this subsection (b) shall be
10 of such sound value as reasonably to assure repayment."

11 SEC. 4. Section 306 of the Small Business Investment
12 Act of 1958 is amended to read as follows:

13 "SEC. 306. Without the approval of the Administration,
14 the aggregate amount of obligations and securities acquired
15 and for which commitments may be issued by any small busi-
16 ness investment company under the provisions of this Act
17 for any single enterprise shall not exceed 20 per centum of
18 the combined capital and surplus of such small business in-
19 vestment company authorized by this Act."

Senator PROXMIRE. Our first witness will be Mr. Eugene P. Foley,
Administrator of the Small Business Administration.

Mr. Foley, we are glad to have you here.

I understand that you have Mr. Parris with you, who is an out-
standing expert in the SBIC field.

STATEMENT OF EUGENE P. FOLEY, ADMINISTRATOR, SMALL BUSINESS ADMINISTRATION; ACCOMPANIED BY JAMES L. PARRIS, DEPUTY ADMINISTRATOR, LAWRENCE S. CASAZZA, DIRECTOR, INVESTMENT DIVISION, GERALD S. FISHER, CHIEF, PROGRAM ADMINISTRATION AND COMPLIANCE DIVISION, INVESTMENT PROGRAM; AND LEONARD RALSTON, ASSOCIATE GENERAL COUNSEL

Mr. FOLEY. Mr. Chairman, I have a number of officials from the SBA with me. Mr. Parris, who is Deputy Administrator for the the investment program, Mr. Casazza, who is the Director of the Investment Division, and Mr. Gerald Fisher, Chief of the Program Administration and Compliance Division of the investment program and Mr. Leonard Ralston, who is the Assistant General Counsel in the investment program.

Shall I proceed?

Senator PROXMIRE. Yes, go right ahead. It take it that you have identified these gentlemen not in sequence, but you have identified everybody at the table.

Mr. FOLEY. Mr. Casazza is on my far right, Mr. Parris on my immediate right, Mr. Ralston my first left and Mr. Fisher on the far left.

Senator PROXMIRE. Do you prefer to finish your statement before I interrupt for questions?

Mr. FOLEY. I would just as soon be guided by your desire, Mr. Chairman. What I propose to do here is to read my statement. Mr. Parris is also going to make a statement, and it may be more convenient to question after the conclusion of both of our statements.

Senator PROXMIRE. All right, fine. Go right ahead.

Mr. FOLEY. The primary purpose of these hearings is to determine whether further safeguards should be established against the potential dangers presented by transactions in which a small business investment company extends financial assistance to an affiliated small business concern. The problem we are considering arises where any person has material connections with both parties to the transaction. He may, for example, be an officer or director of each or he may own a significant share of each.

The unfavorable effects which such an affiliated transaction may have on the rights of those shareholders in the SBIC who have no interest in the business receiving the money are, of course, obvious. Also, these transactions may be used to divert to other uses funds appropriated by Congress for the assistance of small firms which cannot obtain long term or equity financing from private sources. Ever present, therefore, is the chance that the interests of the SBIC or of the taxpayer are being disregarded.

In view of these hazards, it is not surprising that suggestions have been made from time to time about the desirability of issuing a regulation imposing a flat ban on affiliated transactions by SBIC's. But the agency has always been stayed from such action by the force of other considerations. Mr. Parris, Deputy Administrator for the Investment Division, is much more familiar than I with the details of this matter. After I complete my brief statement on the subject, I am

going to ask him, subject to your permission, Mr. Chairman, to discuss the legal and factual background involved. My purpose here is to summarize the situation and to state the position of SBA.

The salient feature of the problem is that there are many parts of the country in which a small businessman does not have a reasonable range of choice in seeking an SBIC to assist him in meeting his long term and equity capital needs. In some communities, indeed, there may be only one company to which he can turn. If he happens to be an investor in that company, or if he serves as an officer or director of it, a ban on affiliated transactions might cut him off from all hope of assistance.

Since such relationships are by no means uncommon between a small business concern and the only available company, SBA decided that, instead of an outright prohibition, it would permit affiliated transactions under a screening procedure designed to insure against abuses. Accordingly the regulations of the agency—13 CFR 107.716—require advance clearance for financial assistance extended by SBIC's to small firms wherever any person enjoys a significant degree of ownership or control in both parties to the transaction. Approval is given only to those proposals which promise to promote the purposes of the program.

The policy represented by this screening procedure is, in my opinion, entirely sound. I intend to continue it. However, I am fully aware that, unless it is administered wisely, it will be harmful to the program. We must have sufficient insight to anticipate the types of abuse most likely to be attempted. We must develop effective methods of detecting and frustrating such attempts whenever possible. I am also aware that we must be tough with persons responsible for abuses. It is imperative that such people be promptly expelled from the program and subjected to whatever punishments the law may have in store for them. You will not find me hesitant or squeamish in dealing with violators.

I am having a survey made of SBA's methods of handling the problem of affiliated transactions to determine whether they meet the standards I have just described. Although the survey has not yet been completed, it is already evident to me that two changes in our procedures would be desirable in order to provide the industry, and the public generally, with more information as to our methods of operation.

First, the criteria employed by SBA in deciding whether an affiliated transaction should be permitted are going to be published. Every proposal must meet all of these tests:

A. Are the shareholders in the SBIC who have no interest in the recipient of the financial assistance in a position to block the transaction if they wish to do so?

B. Is the proposal fair and reasonable?

C. Would the proposal serve the purpose of the program?

These criteria are of necessity so broad that they can serve merely as general guidelines for an SBIC contemplating an affiliated transaction. It is entirely a matter of judgment, for example, whether a transaction meets the test of being fair and reasonable. Nevertheless the industry should be apprised of the broad factors we consider in passing upon applications.

The second change to which I refer relates to our rulings on applications to permit affiliated transactions. In order to provide further guidance for the industry these rulings will be made public, together with all of the facts essential to an understanding of them. SBA has always followed the practices of giving confidential treatment to business data submitted by applicants for loans and other forms of assistance. Revelation of such data can, of course, be harmful to the concerned affected. This is particularly true when they are in a growth period—typical, of course, of so many small firms receiving assistance from SBIC's. It is equally true when they are competing intensively and successfully in a specialized area against large concerns.

It seems to me, however, that such harm can be avoided by following the pattern established by the Internal Revenue Bulletin which, while publishing the facts upon which each tax ruling is based, conceals the identity of the person or firm involved. This is the procedure I plan to adopt.

Let me emphasize that SBA has ample authority under existing law to cope with the problems attending affiliated transactions. We can and will impose any further restrictions on them that may prove to be appropriate. If necessary, we can eliminate them entirely. The flexibility offered by this regulatory method of control is highly desirable and should be retained. For these reasons I would be strongly opposed to any legislative proposal seeking to displace such flexibility with rigid rules.

Although I am not as yet familiar with all of the technical details of the small business investment program, I know enough about it to recognize its vast potentials. I am determined to do all that is in my power as Administrator to strengthen and expand this credit medium and to obtain for it a secure position in our banking system.

Senator PROXMIRE. I want to come back of course to detailed questioning later. I would want to ask one question right now before we go on with Mr. Parris.

Do you plan to provide any explanation of how the general criteria were applied in specific cases?

Mr. FOLEY. Yes.

Senator PROXMIRE. For example, in each case, when the self-dealing approval is given, will you publish that in this particular case your general criteria were applied and how they were applied in that particular case.

Mr. FOLEY. That is what we propose.

Senator PROXMIRE. This is a change from the previous policy?

Mr. FOLEY. We propose to do that without identifying the concern.

Senator PROXMIRE. Without identifying the concern?

Mr. FOLEY. Without publishing the name of the companies involved, this is similar to Internal Revenue system that I referred to in my statement.

In other words, what the Internal Revenue system now does, and what we propose to do is to publish how the general criteria were applied in a given case without identifying the name of the company or concern involved in that particular case.

Senator PROXMIRE. How can there be any public scrutiny of your administration of this program?

Mr. FOLEY. I think there can be scrutiny in the sense that our judgment as to the application of the criteria would then be under public scrutiny.

Senator PROXMIRE. Not if we don't know what the case is.

Mr. FOLEY. I plan to adopt the procedure used by the Internal Revenue Service, Mr. Chairman, all of the facts are given except the name of the company. We have all of the facts. You would have all of the facts we would have in making a determination whether affiliated transactions should be permitted with the exception of the name of the company.

Senator PROXMIRE. You give all of the details on the company, its size—

Mr. FOLEY. We give the details—

Senator PROXMIRE. Its type, interest, the kind of business it is in, et cetera. That is public and public knowledge and subject to public scrutiny. You don't give the particular city in which it is located?

Mr. FOLEY. That is correct, we would not give the name of the city.

Senator PROXMIRE. So that you would not have any of the most predictable and effective kind of scrutiny which would come from the particular community in which it is located; local newspaper, local competitors, and so forth who might take an interest and who would want to be protected.

This would require a kind of national scrutiny of the whole thing which we might rely on the Wall Street Journal, New York Times, or some other national institution.

Mr. FOLEY. That is correct.

Senator PROXMIRE. I see.

Mr. PARRIS, go ahead. I presume you are through.

Mr. FOLEY. Yes, I am; thank you.

Senator PROXMIRE. Very good statement.

Mr. PARRIS?

Mr. PARRIS. Mr. Chairman, as Mr. Foley has pointed out, I will sketch for you the considerations that led SBA to adopt its self-dealing regulation covering transactions between an SBIC and affiliated persons. Briefly summarized, section 716 of the regulations promulgated under the Small Business Investment Act of 1958 provides that a licensee may not, without the prior written approval of SBA, make a loan to or invest in any small business concern which is affiliated with the SBIC by reason of any combination of common officers, directors, or 10 percent or more stockholders, nor may a licensee provide such financing directly to any of its officers, directors, or 10 percent or more shareholders. Since the inception of the SBIC program, the agency has, of course, been aware of the thorny problems raised by these transactions. The agency sought guidance, first from Congress itself.

As the committee knows, the Investment Company Act of 1940, the 1940 act, is quite specific on the question of affiliated transactions, whereas the Small Business Investment Act is completely silent on the point. We do not think that this was an oversight on the part of Congress.

In writing the 1940 act, Congress included a provision of section 3(c)(1) which excepted from all of the provisions of the act, including the provisions covering affiliated transactions, any investment

company whose securities were beneficially owned by not more than 100 persons. Congress apparently felt that security holders in the smaller investment companies did not require the protection afforded under the 1940 act to security holders in larger companies.

Evidently the rationale was that the public interest was not sufficiently affected by the operations of the small investment companies to justify placing heavy administrative burdens on the Securities and Exchange Commission and these small investment companies. Congress recognized that such burdens would result if the SEC had to regulate all of the small investment companies as well as the larger ones. In adopting the 1940 act, Congress evidently concluded that security holders in closely held investment companies would be sufficiently able, with the assistance of State law, to take care of their interests without the help of the 1940 act and the SEC. In doing so, Congress was following a pattern evident in many laws of excluding the smaller units of an area being regulated. You gentlemen are familiar, of course, with such provisions as are included in the wages and hours laws, and various labor-management acts such as the Landrum-Griffin Act.

It will be recalled that in acting on the Small Business Investment Act, Congress considered and rejected a proposal to exempt SBIC's from all of the provisions of the 1940 act. Congress determined that any SBIC that fell within the definition of an investment company under the 1940 act and which did not qualify for the exception provided in section 3(c)(1) of that act less than 100 stockholders should be subject to all its provisions, including the provisions covering affiliated transactions.

Congress, by so doing, thus determined that the smaller SBIC's, for example, those with 100 or less security holders, should not be subject to the provisions of the 1940 act. By deciding not to include a provision covering affiliated transactions in the Small Business Investment Act, Congress seemed to be saying that the smaller SBIC's should not be statutorily covered by any provisions in the area of affiliated transactions. This was consistent with the intent of Congress as expressed in section 3(c)(1) of the 1940 act, mentioned above.

As far as we can determine, Congress appears to have dealt directly with the question of affiliated transactions by the smaller SBIC's only in connection with the granting of certain exemptions from the personal holding company provisions of the Internal Revenue Code. Speaking on that matter, Senator Sparkman, in introducing a bill, S. 3481, in June 1962 to amend these Internal Revenue Code provisions, stated that the basic provision of the Internal Revenue Code, that any SBIC which provides funds to a small business concern in which one of its shareholders owns a 5-percent-or-more proprietary interest loses its personal holding company exemption, was recognized as an effective deterrent against this practice of self-dealing. In summary, the agency was faced at the outset by general congressional silence with regard to affiliated transactions by smaller SBIC's.

Another fact considered at that time was that this was a brandnew program, not only in terms of legislation but also in financing theory. Thus, SBA was faced with the problem of creating interest in and generating the growth of this new financing system. It was recognized that the primary source for licensee applicants would be from busi-

nessmen themselves in any given community. In any area they represented an important initial source of funds for the formation of SBIC's, perhaps the principal source. Logically then, a small business concern in a remote region would not have been able to obtain venture capital funds from any source if it were denied access to the local SBIC because of an affiliation. SBA realized that this problem might well have been acute, since the prominent citizens who were most likely to be directors of a number of local concerns were precisely those who were also most likely to form a small, locally oriented SBIC. These facts had to be considered in connection with any rule prohibiting transactions with affiliated persons.

Another problem involved in the creation of the typical SBIC was the recruitment of qualified management personnel. It would have made little or no sense to look outside the community for someone to manage the company, especially since there was no immediate prospect that the volume of work on a \$300,000 company would justify a full-time job. The natural solution was to draw upon local talent, the small businessman of the community, to serve as officers and directors. Had these men been told by SBA that such service would automatically render their own firms ineligible for assistance from the SBIC, they would have shied away from the SBIC program.

In the unlikely event that the founders of the SBIC succeeded in organizing their company, in the face of the difficulties I have mentioned, a ban on affiliated transactions would have hampered it severely in finding opportunities for profitable investments. Deprived of some of the best prospects in the neighborhood, its chances for success would have been slender. Moreover, we have found that generally it takes some time for an SBIC usually to make its first investment and break the ice. Perhaps the very venture capital nature of the program causes the management to be extra careful about the first investment. To be able to negotiate a deal in an area of personal knowledge or with a locally known concern was a natural development from the businessman's viewpoint.

Furthermore, the agency was hesitant to impose on the initiators of the fledgling SBIC industry any requirement substantially more stringent than they would face in the case of other investments. In view of the basic nature of the SBIC program, it was thought that it would be a real hardship to adopt rules in this area or other areas that would have constituted a sharp departure from corporate practices not elsewhere regarded as abnormal.

It is, of course, true that under all State laws, minority stockholders have remedies available to them in the event they can prove abuse of trust by corporate management. However, the courts have recognized generally that if a disinterested majority of a board of directors approves a transaction, it is usually valid even though a director on the board has a private pecuniary interest in the transaction.

Moreover, any decision to bar transactions involving more than a specified degree of affiliation would have called for a prescience as to the pattern which SBIC negotiations and transactions would follow, a knowledge which the agency felt, would be foolhardy for it to presume. This matter of affiliated transactions is a complex one affecting all phases of corporate life. Even after countless cases, the

State and Federal courts have been able to evolve only general principles and guidelines. This problem is accentuated substantially when it occurs in the context of a new and dynamic program involving Government funds, substantial capital risks, and an infant financial institution such as the SBIC.

Finally, the agency did not want to establish any flat prohibition against a particular type of transaction until it had had the benefit of experience in administering the program. SBA felt, as the Congress itself felt, that the program was experimental in nature and the agency did not wish to hamper it with restrictions which might prove to be unduly oppressive. SBA was particularly mindful of the necessity for allowing this new form of investment company the greatest possible flexibility, within the bounds of congressional intent, in arriving at its business decisions. In short, SBA did not believe it wise to rule out all affiliated transactions or any other type of transaction that might make significant contributions to the SBIC program.

Nevertheless, the agency was not prepared to allow such arrangements without careful scrutiny on an ad hoc basis. Despite the absence of any specific provision in the SBI Act concerning transactions between an SBIC and affiliated persons, SBA concluded at the inception of the SBIC program that it should have a regulation requiring prior SBA approval before such transactions could be consummated. The agency felt that there were sufficient possibilities of abuse in this area to warrant careful scrutiny. Moreover, the presence of Government funds and of tax benefits seemed to justify the inclusion of a provision guarding against abuse in this area, even in the absence of congressional language calling for such a provision.

Thus, pursuant to the authority granted in section 308 of the SBI Act to prescribe regulations governing the operations of small business investment companies, and after weighing all the elements mentioned above, SBA adopted such a regulation in December 1958. The regulation cited earlier has been on the books in substantially the same form ever since the first SBIC regulations were adopted.

In administering this regulation, SBA has attempted to minimize as such as possible the administrative burdens that such a regulation imposes on the SBIC's, the small business concerns, and SBA.

Thus, the agency determined to process requests for approval of affiliated transactions without the abundance of paperwork characteristic of procedures based on public notice, action by order, and full disclosure. Instead, to insure expeditious handling and consonant with its responsibilities to the SBIC's, to small business concerns, and to the objectives of the program, SBA has relied on letter application of the SBIC's and such additional data as it deemed necessary or appropriate.

In determining whether to grant approval of a proposed affiliated transaction, SBA has evolved criteria that are quite similar to those Congress itself provided for with respect to such transactions in section 17(b) of the 1940 act, and to the criteria generally applied under State corporate laws. At the same time a policy was adopted that approval would be given only to those proposals that promise to promote the purposes of the program. A careful and probing reexamination of SBA decisions to date does not, in the opinion of my staff and

myself, reveal evidence of perversion of congressional intent. We believe that, in the light of the compelling considerations I have summarized above, the policy the agency established was thoroughly justified. Consistent with our policy of continually reviewing the SBIC program, this particular area was reevaluated last fall.

I would like to emphasize that this reevaluation considerably predated the recent interest in the problem manifested in the press; indeed, SBA has been set up, on a continuing basis, a staff committee to revise the agency's regulation under the SBI Act in toto, and the agency has also had occasion to consider this problem in connection with pending legislation.

The agency's regulations under the SBI Act were amended in a number of respects during the spring and summer of 1962. As a result of suggestions from Members of Congress and from the industry, SBA felt that the further issuance of a number of separate regulations, in piecemeal fashion, would be unsettling and burdensome to the industry. Accordingly, we consolidated all amendments to the regulations through September 1962 in a new set of regulations, and a staff committee was given the task of developing an overall revision of the regulations.

This committee held meetings from time to time for a period of some months and made substantial progress with the overall revision. A tentative redraft of our regulation on the subject of affiliated transactions was included as a part of the overall revision.

In view, however, of pending legislation on the SBIC program—S. 297, S. 298, and S. 1427, together with companion bills in the House—together with the critical posture of the SBIC industry at that time, SBA concluded that priority should be given to legislative matters. Accordingly, the work of the regulations committee was discontinued in the early part of this year with the understanding that the project would be resumed when the legislative situation had been clarified.

In tabling this matter, we also were generally aware that the amount of financial assistance involved in such transactions had not been particularly substantial. Our most recent figures show that outstanding loans and investments approved by SBA under section 716 of the regulations amount to only 1.6 percent of the total SBIC financing on the books.

As a result of these studies and discussions, as well as SBA experience in administering its regulations in this area, we have come to the conclusion that the policy represented by this screening procedure appears basically sound, factually justified, and consistent with the broad purposes and goals of the act.

Senator PROXMIRE. Now, at the very end of your statement, next to the last paragraph, Mr. Parris, you answer a question I was all set to ask you. It seems to me you answer it in a way, that is you say only 1.6 percent of the total SBIC investments involve any consideration under section 716 of the regulations, which I presume means the self-dealing regulation.

Mr. PARRIS. That is correct.

Senator PROXMIRE. This is really pretty minor. I can't imagine under these circumstances that to either abolish the self-dealing permission outright or to require disclosure to discourage it, would crimp

the SBIC program if less than 2 percent of the loans that have been made throughout the years—you have had this program now for 4 or 5 years—less than 2 percent of those loans involve this, why would this inhibit outstanding citizens, bankers, and others, all of whom we would like to have as members of the SBIC, from forming an SBIC? Apparently this program is working very well, 98 percent plus in the direction of making loans, as at least I think they should make them, to others who are not members of the board of the SBIC. Now, if this is the case, why do you really have to have this loophole in view of the possible scandals that could develop, in view of the adverse effect on stockholders involved, minority stockholders, and in view of what I think is a first class but critical article in an outstanding financial publication, the Wall Street Journal. Do you want to answer that?

Mr. FOLEY. Do you have any objection if I venture a reply?

Senator PROXMIRE. Fine. Incidentally, when I direct a question, or any of us do, I am sure we would be delighted to have either one of you answer.

Mr. FOLEY. The distinction has to be kept constantly in mind between the smaller SBIC's and larger ones. Obviously, the 1.6 percent figure refers to all of the SBIC investments put together. But the substance of Mr. Parris' statement as well as my own referred to the problems attendant on the smaller SBIC's. I don't think it would be the intent of Congress, surely not the intent of our agency, to put inhibiting factors into smaller SBIC's.

Senator PROXMIRE. Let's get into smaller SBIC's. In the first place how many SBIC's are there?

Mr. PARRIS. 676 active, as of August 31, 1963.

Senator PROXMIRE. And about how many loans do these SBIC's make, or investments?

Mr. PARRIS. Outstanding balances for loans and investment as of March 31, 1963, were about \$387 million.

Senator PROXMIRE. How many in numbers?

Mr. PARRIS. You mean transactions?

Senator PROXMIRE. How many transactions?

Mr. PARRIS. About 7,000.

Senator PROXMIRE. Now the Wall Street Journal article reported from last October—admittedly this is a short period, from October to May—that there were 36 applicants for applications for self-dealing approval. Thirty-three were granted. If this was a representative period, I presume that this would mean that there were about 60 a year, and hence that this would constitute, in terms of the number of transactions involved, a small percentage.

Mr. PARRIS. That general conclusion is correct. It is a small number of transactions.

We have had a little more time to go over our records since those days, and we have found the numbers are somewhat higher. But basically the figures since June 30, 1963, in fiscal year ending June 30, 1963, we have had 56 approvals and 15 denials.

Senator PROXMIRE. Can you give us the benefit of the full record now—is that available—of all of the self-dealing applications that have been made, and the approvals that have been granted from the beginning of the program? Is that available to us?

Mr. PARRIS. By that do you mean statistics?

Senator PROXMIRE. Yes, sir.

Mr. PARRIS. That is available.

Senator PROXMIRE. Do you have it available at your fingertips?

Mr. PARRIS. Yes, sir.

Senator PROXMIRE. Read them off, please.

Mr. PARRIS. Actions on requests for approval investments, under section 107,716(b) by fiscal year:

For the fiscal year ended June 30, 1960, there were no denials; 15 approvals. Dollar amount of the approved loans was \$843,900.

Senator PROXMIRE. For the full fiscal year?

Mr. PARRIS. Yes, sir.

Senator PROXMIRE. All right.

Mr. PARRIS. June 30, 1961—fiscal year ended June 30, 1961: 4 denials; 32 approvals. Dollar amount of approved loans was \$2,056,833.

Senator PROXMIRE. All right.

Mr. PARRIS. Fiscal year ended June 30, 1962: 9 denials; 43 approvals. Dollar amount of approved loans, \$2,864,897.50.

Fiscal year ended June 30, 1963: 15 denials; 56 approvals. Dollar amount of approved loans was \$4,010,966.72.

The totals through June 30, 1963: 28 denials; 146 approvals; \$9,776,597.22 being the aggregate dollar amount of approved loans.

(A tabulation of the above figures follow:)

Actions on request for approval of investments under sec. 107.716(b), by fiscal year

Fiscal year ended—	Denials	Approvals	Dollar amount of approved loans
June 30, 1960.....	0	15	\$843,900.00
June 30, 1961.....	4	32	2,056,833.00
June 30, 1962.....	9	43	2,864,897.50
June 30, 1963.....	15	56	4,010,966.72
Total.....	28	146	9,776,597.22

Senator PROXMIRE. You say there have been 7,000 loans made altogether by the SBIC's for a total dollar amount for how much?

Mr. PARRIS. \$9 million—

Senator PROXMIRE. I am not asking for this figure, the total. I want to compare this with the total amount of transactions.

Mr. PARRIS. About \$380 million.

Senator PROXMIRE. How much money is involved?

Mr. PARRIS. About \$380 million. The exact figure is \$386,937,466. These are outstanding loans and investments, giving a ratio of 1.6 percent.

Senator PROXMIRE. In terms of the number of transactions it is about 2 percent: 146 approved out of 7,000 transactions.

Once again, it would indicate about the same ratio or, roughly perhaps, at least for the small ones as for the big, and it would indicate, in general, this is a very modest part of the program, and, hence, again I press my argument that under these circumstances that the discontinuation of this program or its modification could hardly be considered to be an action that would discourage people from becoming active in SBIC's.

I think a lot of us are concerned about the notion that people would just start an SBIC and get Government money for the very purpose of loaning to themselves, and I am delighted to see that these figures indicate that a very small minority are even involved in self-dealing; so obviously an insignificant number have that kind of motivation. Most people have the motivation, I think, that we would certainly favor, which is to start an SBIC to help the community, and to go into business to help yourself, too, by making money out of the SBIC.

Doesn't that seem logical, Mr. Parris, or Mr. Foley?

MR. FOLEY. I agree with you, Mr. Chairman.

I don't think the problem is one that requires legislation. I think the scope of the problem is such that it can be handled adequately administratively.

Once again, I do believe that we do have a problem with the smaller SBIC's. I don't think it is the intent of Congress to restrict the SBIC program to big SBIC's. I think new small SBIC's have problems typical of any small business organization, and in trying to assist them in developing their investment program and portfolio, we think that administratively we can review these affiliated transactions and determine whether there is improper self-dealing or whether or not the purposes of the program are being advanced.

Senator PROXMIER. Once again, I am going to defer to my colleagues but, once again, you can look at it from the standpoint of saying this isn't much of a problem because not much money is involved and not many transactions in the relationship of the whole operation.

I would look at it from the standpoint of saying therefore we can take this action without seriously crippling the program. You say therefore it can be handled administratively, and it hasn't been a serious problem in the past. I think some of the instant cases raised by the Wall Street Journal would concern me very much, particularly the possibility of investing in real estate ventures, and so forth, in a way that is described there.

I do want to ask something else, if I could, before I yield to Senators Dominick and McIntyre.

In the Wall Street Journal article this point is raised, and let me read it briefly, one paragraph:

How much information the SBA does demand of applicants remains obscure. Its officials say they do not normally attempt on-scene investigations before approving self-deals, though traveling examiners may later look into them during routine checks made every year or two. Washington operates mainly by correspondence. And its letters of approval seen by reporters merely recite back to the self-dealing SBIC the same information the SBIC has provided. Sometimes Washington takes months to make up its mind. But SBA took only 2 days to clear a deal for Chicago Capital Corp.; a director of this SBIC happened to be partner in a law firm serving as legal counsel for a company which obtained a loan—

And so on.

And it is indicated that one disappointed applicant indicated:

If the SBA was justified in turning down this loan, it should have turned down a lot of the others it has approved. I think a lot of SBIC's have gotten loans that were the same kind as mine. It might be that some of the others didn't furnish full information.

Just how comprehensive is the information? Are there on-scene investigations if the application is above a certain size, and so forth?

Mr. PARRIS. Mr. Chairman, we make no on-the-scene examination in connection with such an application. However, we have a Program Administration and Compliance Division which has people experienced in bank-type examinations. We have a continuing schedule of examining companies, and we have examined quite a few.

The examinations include a check of representations made to the agency and where we find that a misrepresentation has been made to the agency we take action.

There are about a dozen companies that have voluntarily left the program because they realized that it would be in their best interests to leave, as well as the best interests of the program, because they had done things that were substantially out of line with the program.

Moreover, we have formal investigations pending that have stemmed from these examinations. We are also in court on a couple of cases. In one case we have gotten a permanent receiver.

Senator PROXMIRE. These are all cases—where you run into trouble, these are all cases involving self-dealing?

Mr. PARRIS. The case that we got the receiver on involved self-dealing without approval to the extent that it really was a misappropriation, we believe. The full trial has not been held, but a preliminary receiver has been appointed on our allegation that, in effect, it was misappropriation.

Now, in addition, we get information in the licensee's letter requesting approval, and if we deem it inadequate we request additional information. And, in a number of cases, we get additional information.

On top of that, we know a good deal about these companies before they come in. They go through a very complicated licensing process in which we make checks on their credit, character, and we have quite extensive Government facilities and normal commercial investigation facilities to do so.

Senator PROXMIRE. Is the story inaccurate when it says this particular loan was made in 2 days—was approved in 2 days?

Mr. PARRIS. That one is not inaccurate. There were a number of directors in the company who were disinterested, and there was no financial overlap; merely an attorney who happened to be a director of the company. And obviously there were a great number of disinterested directors who had a substantial financial stake in the loan, who were passing on it.

The important thing, Senator, I think that one would not discern readily from the Wall Street Journal article is that we don't pour money into these companies; we lend money. Over and over again that article refers to pouring money, and putting money. We lend money, and the obligation to the Government comes ahead of their private funds. If there are losses the licensees stand them first. And when these men pass on these transactions, they are passing on their own money, at least \$150,000 of their own money, before they get Federal money.

Senator PROXMIRE. Not necessarily their own money; money of their stockholders.

Mr. PARRIS. In many of the smaller companies there is quite an overlap between directors and stockholders, or—

Senator PROXMIRE. You see, we have the problem with the SEC-administered company, that it is all their own money, not a penny of Federal money; yet they prohibit self-dealing flatly.

Mr. PARRIS. On so-called upstream loans, as I understand it, I am not expert in SEC, these are prohibited. But on purchases and sales of securities—and we have debt securities that are more than straight loans—there is no flat prohibition in the SEC act either.

Senator PROXMIRE. You have three criteria which are required: (1) noninterested persons passing on it; (2) fair and reasonable—which is admittedly very vague and general; it could be almost anything—and (3) the purposes of the small business act, which is equally vague. So the only really firm criterion you have is they are noninterested persons.

You and I know in our relationships with each other in almost every experience we have in life, when you are dealing with people who serve with you on a particular board, and they come around for a loan, they want a loan, and they are one of 5 or 10 people who are active and make the decisions, it is an awfully hard thing to say no to them. It is the hardest thing in the world to say no. Sometimes, in some cases, you have very strong-willed individuals who will say no to anybody in any circumstance; or maybe they are just opinionated people who do that. At any rate, they are the exception.

But the kind of situation you have here, the kind of subtle, close personal relationship, is, it seems to me, very difficult for most people who want to be friendly and get along with their colleagues and friends to say no, we won't give you a loan.

So that there is really no protection, it seems to me, in the noninterested person category, especially in the smaller companies.

Now it is true that you go over these things, but you have indicated in your answer to me just now that you rely primarily, and you have to, on this one criterion, whether they are noninterested persons involved, legally defined, and strictly defined as people who wouldn't get a benefit from that particular loan. But actually the personal relationship is really what makes the so-called noninterested persons in most cases unwilling or unable to impose their power on their colleagues and go along rather than raise a fuss.

Isn't that a problem?

Mr. PARRIS. It is a problem, Mr. Chairman. But the courts have faced this problem many, many times, and this is the test that they use.

I am not a practicing lawyer at the moment, but I come from corporate law practice, and I have seen countless cases where this test has been used. And although it is a problem, we have to face up to the facts of corporate life, and we are trying to make this program as close to corporate life as we can.

We don't want the Government all over the place in the program. The whole idea was to get away from direct Government loans, to get private participation. And if we are going to achieve that result, we have to face the facts of corporate life. And the courts have adopted this test over and over again. And when it comes to putting out money, I have seen a lot of businessmen who can be pretty hard-nosed even with their friends.

Senator PROXMIRE. That is right. But there is that problem.

Now how about this as a solution. We haven't discussed this—and this is the last thing I want to question you on.

What really is the difficulty with disclosure? Why isn't disclosure all right? People always say, the small businessman can't disclose what he is doing, he doesn't want to, because it will hurt him in competition.

The fact is in Wisconsin we have had for years—it was knocked out, unfortunately, but for many years we had a provision that income tax returns, personal and corporation, are available to anybody; anybody can go in and look at them. And it worked very well. The fact is that nobody was embarrassed. The argument was made, I am sure, insurance salesmen and others would come around and use this to develop lists, or they would be used by competitors in various ways. It was a very salutary law that helped keep our State clean and keep criminal elements out, and enforced very inexpensively the income tax law.

Now in view of the fact that self-dealing is rarely engaged in—the statistics show it is rarely done—only 2 percent of your transactions are involved, when it is done, when this exceptional situation is involved, what is the matter with letting the public know?

It seems to me if it is completely honorable and fair, nobody should be afraid to have the public know that they are borrowing from their own SBIC.

Mr. FOLEY. Mr. Chairman, remember this program, of course, is for small companies, for small businesses. The typical small business, the typical small SBIC is dealing with—is a venture or risk-taking enterprise. The moneys that are advanced to that enterprise are enabling that firm either to begin operation or to grow.

In such a situation there is a great risk of failure. This is to be contrasted with the situation of a larger company which, when it obtains venture capital, is really risking immediate failure. There is a difference and it is not just in degree. It is a difference in nature between the venture capital that is required by a small company as compared to that required by a large company.

Consequently we feel that the smaller company ought to be protected in its confidentiality so that suppliers are not scared out of that firm's operation, or so that competitors could not take unfair advantage of the risk position of that small company.

Senator PROXMIRE. Here we have a specific instance in the Journal article, and it seems to me that in no case, none of these cases, should it matter, if the loan was perfectly honest and honorable and proper, should it matter to the person borrowing the money if the public knows about it. And I haven't heard a single—I have heard persuasive and eloquent generalities—but I haven't heard a single practical instance of how a particular firm in a particular case would be injured or hurt or discouraged if the details had to be revealed.

Mr. FOLEY. I think the danger there, Mr. Chairman, is that if we overregulate this program—

Senator PROXMIRE. I am asking about disclosure. Then you don't have to have all of this?

Mr. FOLEY. Let's say we have disclosure or increasingly rigid regulations: I think there is danger here that the Government is going too far in exercising its judgment as to what the competitive situation of the small company would be.

I think there has to be a certain small area here of fluidity. These things aren't black and white. We in our agency don't have the omnipotence to determine in each case the competitive situation of a particular firm in Seattle or Boston. There has to be a certain bit of freedom here for the company to operate without fearing that it is going to disagree with the judgments of somebody in Washington.

It may be a generality, but I don't think it is wise generally for a Government agency to be supervising each transaction that a company undertakes.

Senator PROXMIRE. I couldn't agree with that more. That is exactly why I think disclosure is helpful. Then if there is disclosure, local people know, local newspapers, local bankers, and competitors and others, if there is something wrong with it. Then it is more likely to be corrected than if the whole burden of enforcement is on the Government official here in Washington who must pass on it, on the basis of correspondence, without visiting the scene.

You see, disclosure, it seems to me, would go right along with the philosophy which I think you are properly enunciating: you should have as little governmental interference and as much private discipline as you can possibly achieve in this kind of a program.

Mr. FOLEY. I just think we are at an impasse, Mr. Chairman. I can't express it any further from what I have already done. I just think a private enterprise ought to have an area of privacy, and I don't think that it is necessary for the whole community or society to know everything that is going on in that company any more than it is in your private home.

Senator PROXMIRE. I am not asking that. All we are asking is that the details of this self-dealing be revealed; not their income tax, their profit picture, or any of that. All we ask, when this is done, is that the public know about it.

Mr. FOLEY. In a small company we are revealing all that. Or the chances are that we are going to reveal most of it. I just think that there ought to be an area of privacy in business life as well as in private life.

Senator PROXMIRE. Maybe I will come back to that. I have detained Senator Dominick and Senator McIntyre too long.

I yield to Senator Dominick.

Senator DOMINICK. I was somewhat interested in the statement made by Mr. Parris here on page 4 of his statement, the bottom paragraph. You say in here—

* * * a ban on affiliated transactions would have hampered it severely in finding opportunities for profitable investments.

Then you go on to say—

Deprived of some of the best prospects in the neighborhood, its chances for success would have been slender.

Why is it necessarily true that the best prospects for success are in affiliated transactions?

Mr. PARRIS. What we meant by that, perhaps it could have been stated more clearly, Senator Dominick, was that a small company is certainly likely to have a better knowledge of its community, and industry and business in that community, than it will in some business several States removed. And yet when it turns in to its own community, especially if it is a small community, it is a very close-knit

proposition in many places in the sense that a few prominent citizens head up not only the charitable activities of the town, but they head up leading businesses. And you get an attorney, a couple of the best attorneys in town will be in a number of things. This is likewise true of the local banker. Likewise true of other local businessmen. And that is what we meant by that, sir.

Senator DOMINICK. What you are really saying is that it would limit the scope of their possible investments. Isn't that it?

Mr. PARRIS. Yes, sir.

Senator DOMINICK. You are not really saying that these are the most profitable simply because they are affiliated?

Mr. PARRIS. No, sir.

Senator DOMINICK. I would like to go on just a little further along this same line.

Do you set up any regulations that when an affiliated transaction is looked at by the SBIC that you require that when the board has approved this type of loan in an application for approval of it, that the board member must be absent from the meeting or that there is a disclosure of the interest of a board member and to the other stockholders before the application is made? Do you make any of those requirements?

Mr. PARRIS. Most of the applications were mentioned where the vote is so large that it didn't make a difference. We don't always press the point. Sometimes the board will be 26. We have boards of 26 businessmen, and 1 interested party. Usually they will abstain. But we always make the number count to make sure that there was a majority of disinterested parties.

Senator DOMINICK. I think I should make my own position clear here for the minute. I don't think simply because a member of the board of an SBIC also happens to be an officer or a director of a company which receives a loan from it, that there is necessarily anything crooked in it. In many cases this is an opportunity to do something for the community as a whole. So therefore I don't think there is anything necessarily crooked in it.

But I can certainly see—

Senator PROXMIRE. I agree with the Senator from Colorado.

Senator DOMINICK. There may be a conflict of interest somewhere along the line unless he does not participate in the decision of the SBIC as to whether or not this loan should be given.

And along that line, I wonder if you have any statistics which would indicate whether these affiliated loans have gone sour anywhere along the line?

Mr. PARRIS. We have statistics that would indicate that most of these loans have not gone sour. The great majority have not.

Senator DOMINICK. Could you furnish to the committee perhaps a comparative list of those which have been successful and those which have not, and the proportion of them with respect to affiliated loans as opposed to nonaffiliated loans? Could you do that for us?

Mr. PARRIS. We will attempt to provide that. I don't know that our reports are quite as precise as you are getting at, but we have a very good idea already that, as I said, the great majority are not delinquent.

We will attempt to get it just the way you ask for it, sir, and provide it for the record.

Senator DOMINICK. Would that be satisfactory?

Senator PROXMIRE. That would be fine.

I think it would be very helpful if you give us all the data you have on each of these loans from the standpoint of their present status, whether or not they are in default at all, and have been repaid, and so forth.

Indicate to us right now, incidentally, if you can, how much work this is. We don't want to impose an impossible burden. There are only 146 loans. I presume that can be done by one or two people in a relatively short time. Now, if it is too much, maybe we ought to reconsider how much of that we want.

Mr. PARRIS. May I ask the man who will have to do the job to answer the question?

Mr. Fisher.

Mr. FISHER. Mr. Chairman, we have information on each one of these companies as to whether or not they are delinquent. We require this information quarterly. We can prepare it.

As far as the time element involved, 146 companies, it will take at least a week to get this information.

Senator PROXMIRE. That is fine.

(The information follows:)

SMALL BUSINESS ADMINISTRATION,
OFFICE OF THE ADMINISTRATOR,
Washington, D.C., September 13, 1963.

Hon. WILLIAM PROXMIRE,
Chairman, Subcommittee on Small Business,
U.S. Senate, Washington, D.C.

DEAR SENATOR PROXMIRE: During the course of the hearings held by your subcommittee on September 5, 1963, you requested certain information with respect to the current financial status of the affiliated transactions which had been approved by this agency. You will recall that testimony was given that there had been 146 such approvals for a total dollar amount of \$9,776,597.22.

We have reviewed the June 30, 1963, financial reports of the licensees concerned with such transactions and have the following information to report: Of the 146 approvals, 35 of them in the total amount of \$2,819,333, or 28.8 percent of total approvals, had not been disbursed by the licensees. Thirteen investments in the amount of \$635,600 had been repaid in full. There were three affiliated transactions which were reported delinquent as to principal payments in the amounts of \$25,000, \$12,000, and \$7,376, for a total principal delinquency of \$44,376. These principal delinquencies represented 17, 2.9, and 3.5 percent of the respective licensee's outstanding investment balances. In addition, the June 30, 1963, reports indicate that there were five such transactions in which there were defaults in interest in the amount of \$1,337, \$1,282, \$854, \$3,250, and \$4,407, for a total interest delinquency of \$11,130. None of the affiliated transactions had been written off the books of any licensee as worthless.

I think you will agree the foregoing financial information indicates that SBA's policies have been sound with respect to approvals given for affiliated transactions.

Sincerely,

JAMES L. PARRIS,
Deputy Administrator.
By LAWRENCE S. CASAZZA,
Director, Office of Investment.

Senator DOMINICK. Mr. Foley, just carrying along the chairman's theory a little more on disclosure, I must say I subscribe to his opinion on this. I know that in a case where you have any confluence of interest, in an ordinary SEC transaction, this has got to be disclosed in the prospectus, and this has never done anybody any harm as far as I know. You usually have some businessmen who balk at that and say

it is none of the Government's business. But it has never done anybody any harm as far as I can see where the transaction is on the up-and-up.

As a lawyer I had always required wherever we had something of this kind that the stockholders be informed of it. And I can't see that there is any real reason—I am talking about a fundamental business reason, which would say that these transactions should not be disclosed at least to the stockholders and be a matter of record in case anybody wants to look it up in the SBIC office.

I wonder if you could enlarge a little on your reasons.

Mr. FOLEY. Senator, in a typical small company there wouldn't be any difficulty for the stockholder to get the information. We are not trying to prevent this information going to the stockholder. It is just that we are trying to protect the competitive situation of the company receiving the investment.

Admittedly in many affiliated transactions disclosure may not affect the competitive situation. But in other cases we think that it would.

Without being overregulative in attitude, we just think there ought to be an area of privacy here, a little area of freedom for an SBIC to operate in.

Senator DOMINICK. When an SBIC makes a loan in the areas that are announced by the SBIC, are they announced by the SBIC or by you?

Mr. FOLEY. It may be—it isn't required, but there may be announcements and there may not be.

Senator DOMINICK. In many cases it is, though?

Mr. FOLEY. In many cases it is, like any other large transaction.

Senator DOMINICK. I have seen some announced in our own papers. It seems to me if you are going to announce them in those cases there is no reason why you should do it there and not do it in affiliated loan position.

Mr. FOLEY. What we are getting at is, Senator, the details of the transactions are not always announced. The amount of the investment perhaps is announced, but all of the facts attendant on the investment are not published. The other security holders, the other loans that they might have, the tax situation of the firm—all of these are factors that are brought to bear in any large investment in one of these companies. It is this type of information we don't want to disclose.

Senator DOMINICK. I don't think anybody has been suggesting that we need go that far. But it does seem to me that if there was a publication—it doesn't need to be a publication, simply a matter of record, so that people could look at it, where there is an affiliated transaction. It is going to take a lot of ingenuity and work on the part of a competitor to get any value out of this. They are going to have to come back and look at the records here, in the form of the application. They would have to do a lot of things like that that would be fairly substantial.

Mr. FOLEY. Mr. Fisher wants to make a comment here.

Mr. FISHER. Senator Dominick, you may recall May 17 this committee received testimony in this area. One of the larger SBIC's pointed out that its particular field of investment was extremely competitive and that any disclosure of what the small business con-

cern was doing in a given area, what product it was working on, what R. & D. was going into it, would create a problem in that some of the larger companies hadn't thought of these areas, and they were afraid they would go right into the area and just swamp that small business concern out of business.

This, I think, is a real consideration also.

Senator PROXMIRE. Will the Senator yield on that point?

Senator DOMINICK. Yes.

Senator PROXMIRE. We are asking in the alternative proposal that in addition to providing the information that is required now for the administrator, that there be published in a newspaper of general circulation in the locality in which it has its principal place of business a notice setting forth only these things: (1) the nature of the interest or interests requiring the giving of such notices; and (2) the terms upon which the purchase or loan was made.

Now that has nothing to do with the product you might be working on. All it says is you are borrowing so much money over such a period of time at such interest, or whatever other provisions there may be, technical provisions on the security, and it is being loaned to a person who is director or stockholder in the SBIC.

How can that help a competitor? There is nothing about R. & D., nothing about new products, nothing about new fields. And certainly any alert competitor will know this. All he has to do is drive out and look and see you are expanding your plant.

Mr. FOLEY. It could very well reveal the financial strength of the company just by revealing the terms of the transaction.

Mr. PARRIS, do you want to add to the comment?

Mr. PARRIS. I think that the point about small business is particularly well taken when even large business regards some of this area as confidential.

You gentlemen will recall, I believe about a year ago, there was a Senate investigation of the profit picture and the cost of products picture in the steel industry, and a full Senate committee upheld the steel companies in refusing to disclose certain information which, they said, if it got in the hands of their foreign competitors, would make their situation very bad. Well, this problem in a small business would be a very real one. In large business areas this has come up several times to my attention in situations where it didn't sound like general talk. And we don't say all investments are this way, Mr. Chairman, but in the research and development area—this has been one of the big areas of this program, in research and development; and especially in electronics it apparently is a real factor.

Senator PROXMIRE. We are not asking for any cost data. We are not asking for any cost justification. We are not asking for any profit picture. We are not asking for any research or development or any product information at all. All we are asking is that the interest involved in this case be identified and the terms of the security be identified. Every large business of any kind that is public at all reveals this, and it is known widely, whenever any firm wants to borrow money. As a matter of fact, I suspect this kind of thing would be fairly well known possibly in the community anyway. But as a matter of protecting for all those involved, and as a matter of providing the kind of public scrutiny which can be the best substitute for bureau-

cratic interference, it would seem to me that the disclosure is no penalty at all really to a small business firm when it is this limited.

Mr. FOLEY. Mr. Chairman, let me just hedge to this extent and say we do have the authority to handle this administratively. It would have to be my decision. I am not yet persuaded. I agree that I have approached the thing so far with a great deal of generality. It may be that what you have suggested here has some merit and that we could handle it administratively. I don't know that it necessarily requires legislation. Under the terms that you have just outlined, just a limited disclosure that you are referring to, there may be some possibility here.

I would just like to have a little bit more time to live with the program, frankly, to make up my own mind. We do feel—I just feel very strongly that we ought not to be exposing a company entirely to the public. There ought to be an area of privacy. But under the limited area you just outlined, it may be possible we could require by administrative regulation that there be a local disclosure or local announcement of the transaction without really going greatly into the nature of the transaction.

Senator PROXMIRE. The kind of information, for instance, you would require—the vote by which the board of directors approved the transaction, the reason why the purchase of the loan is considered to be a sound investment—none of that would be required. We are not asking for that. What we are asking for is simply the fact that a loan is made to an interested party and the terms of the investment involved. That was the alternative that we prepared.

I am sorry. I have taken the time of the Senator.

Senator DOMINICK. I just wanted to make this comment, Mr. Chairman. In my own legal practice, before I entered Congress, whenever we were going to have a prospectus out on a company, small or otherwise, I always made them put in every possible adverse thing that they could possibly think of in the company, whether it was contingent or whether it was actual, on the theory that a prospectus is an insurance policy against suits by your stockholders. As long as you reveal this thing and it has been publicly revealed to everybody, no one can say you hadn't told them about it.

This is the thing I was thinking about in the disclosure here. You have affiliated transactions. Unfortunately, human nature is such that some of the stockholders in one of the companies, if it goes sour in the company that has the loan, they are going to say this fellow got a special profit out of it, or if it goes bad from the point of view of the SBIC, the stockholder there can say, well, this gentleman got a particular profit out of it. But if it is disclosed and they know all about it ahead of time there isn't a thing they can do about it.

This is what I was thinking about, as a protection, rather than anything else, on the assumption that the directors are going to operate without the particular necessary vote of the interested director or officer whoever it might be.

I think this worthwhile, thinking in terms of the context of your remarks, because what we are trying to do, as I see it, is twofold: (1) To keep the prestige factor of the SBIC as high as we can; and (2) to prevent this from becoming the subject of an attack on a conflict of interest where, in fact, there might not be any.

Excuse me, Mr. Chairman. That is a long monolog.

Senator PROXMIRE. Do you want to say anything?

Mr. FOLEY. I have no further comment.

Senator PROXMIRE. Senator McIntyre?

Senator McINTYRE. I have a few questions.

Mr. Foley or Mr. Parris can answer these.

As I understand it, this type of self-dealing financing occurs in only about 1.6 percent of the total transactions of the Small Business Administration, so conversely this would mean about 98.5 percent do not involve in these situations where you have self-dealing?

Mr. FOLEY. That is correct.

Senator McINTYRE. Therefore, an outright prohibition against any transaction which involves any interlocking interests would not be severely damaging to the whole program, would it?

Mr. FOLEY. We did discuss that a little bit earlier, Senator, and what we referred to there, it would be damaging to the smaller SBIC's. The figure of 1.6 percent refers to the total investments by all companies, large and small. We are dealing here today with the smaller SBIC's and the problems that they have with small companies that they invest in.

Senator PROXMIRE. Would the Senator yield on that point?

Senator McINTYRE. Yes.

Senator PROXMIRE. The fact is on transactions basis it is 2 percent.

Mr. FOLEY. 2 percent.

Senator PROXMIRE. So it means as far as the small firms which make the bulk of the loans in numbers, not in dollars, that once again it would be only 2 percent that would be affected and 98 percent would still be free. So that while the smaller firms might be slightly more involved in self-dealing than the bigger firms, these transaction statistics suggest there isn't a great deal of difference, 1.6 in dollar amount, roughly 2 percent in 146 loans out of 7,000 in transactions, and therefore there is not any really sharp distinction between the activities of the big and the small SBIC's.

Mr. FOLEY. Statistics show we had 146 such transactions, in roughly \$9 million, and to the small SBIC it was an important investment and important consideration for its operation. It isn't a big problem, but nevertheless for the health of the small SBIC's we still think that it would be unwise to have a flat ban against it.

Senator McINTYRE. Mr. Foley, in a previous meeting of the committee I believe that I understood that this type of self-dealing is not allowed in any other agency of the Government except in this Small Business Administration. Is that true?

Mr. PARRIS. I don't think that is quite accurate, Senator, in the sense that the SEC has a flat ban, as I understand it, on loans to people who control the investment company. But they do not have a flat ban on affiliated transactions other than upstream ones—in other words, purchases and sales of securities. In those areas they are, as in our case, banned, unless prior approval of the SEC is obtained. And the SEC, to give prior approval, as I understand it, must find the terms fair and reasonable, consistent with the policy of the company and with the act.

The banks also do not have a flat ban on such transactions. The banks require that a member of the Federal Reserve System, a bank

that is a member, an executive officer may not borrow at all over \$2,500, I believe, but under that, can, if all facts are disclosed to the board of directors.

Also they have a similar rule as the SEC on directors of banks who may have transactions involving purchases and sales provided that it is in the regular course of business and no more favorable to that person than to anyone else. That is one test. The other test, I believe, is that it has been approved by a majority of the board consisting of disinterested directors.

So in all the relevant Federal areas there has been a tendency to avoid flat bans.

Senator McINTYRE. Flat bans?

Mr. PARRIS. Flat prohibitions. They have recognized the need for making some exceptions.

Senator McINTYRE. Because when a person comes to you in a situation like this it is all done in the area of privacy and as you would be treated by any banking institution. That is the same way you handle it.

Mr. FOLEY. What we propose, Senator, is that we might modify our operation to the extent of publishing the judgments or rulings made by the SBA in these affiliated transactions, similar to the manner in which the internal revenue system bulletin publishes tax rules. We feel that obviously there is a public interest in determining whether there are any improper self-dealings in these transactions. We plan to take care of this by publishing the reasons and facts underlying the rulings without identifying the company. We think we can handle it that way and still protect the public.

Senator PROXMIRE. May I ask where you would publish these? The Internal Revenue has this bulletin. How would you publish yours?

Mr. FOLEY. To tell you the truth, Senator, I just made a note on the same point while we were sitting here. I was going to send Mr. Parris a memo on that. I want to have the whole thing laid out by the end of the week. If you would like to have this incorporated in the record, we would be glad to do that. Frankly this was a recent recommendation of mine. After discussing it with the staff we all thought it was a pretty good idea. The details of publication have not been worked out. But it shouldn't take very long to do this, and we can supply it for your record. (See p. 40.)

Senator McINTYRE. No further questions, Mr. Chairman.

Senator PROXMIRE. Thank you very much for excellent responsive testimony. It has been very helpful.

Without objection, I would like to place in the record a copy of my proposed amendment to the Small Business Investment Act relating to this self-dealing problem. I would like to have your comments on this proposed amendment.

(The proposed amendment and Mr. Foley's comments follow:)

PUBLICATION OF INFORMATION CONCERNING CERTAIN TRANSACTIONS

SEC. —. (a) Without the prior approval of the Administration, no licensee shall purchase equity securities of, or make any loan to, any small business concern, if—

(1) an officer or director of such licensee, or a close relative of such officer or director, is an officer or director, or owns or controls (directly or indirectly) 10 percent or more of the stock, of such concern;

(2) any person, owning or controlling (directly or indirectly) 10 percent or more of the stock of such licensee, also owns or controls (directly or indirectly), or is a close relative of any person who owns or controls (directly or indirectly), 10 percent or more of the stock of such concern; or

(3) any person who is an officer or director of such concern or who owns or controls (directly or indirectly) 10 percent or more of the stock of such concern, within six months prior to the making of any such purchase or loan, served as an officer or director, or owned or controlled (directly or indirectly) 10 percent or more of the stock, of such licensee.

(b) No purchase or loan by a licensee requiring approval under this section shall be approved by the Administration, unless it finds that (1) a majority of the board of directors of such licensee has no interest (directly or indirectly) in the small business concern affected by such purchase or loan, except as may be incidental to and consistent with the conscientious performance of the duties of members of the board of directors of such licensee, (2) such purchase or loan has received the affirmative approval of such majority, (3) the terms upon which such purchase or loan are to be made are not less favorable to such licensee than those offered by it to other small business concerns, and (4) such purchase or loan is in furtherance of the purposes of this Act.

(c) Whenever a purchase or loan by a licensee is approved under this section, the Administration shall promptly notify the licensee in writing and cause to be published in the Federal Register a notice setting forth the terms upon which such purchase or loan is to be made, and the nature of the interest or interests requiring the granting of such approval. Upon the making of such purchase or loan, after approval by the Administration, the licensee shall promptly cause to be published in a newspaper of general circulation in the locality in which it has its principal place of business a notice setting forth the terms upon which the purchase or loan was made, and the nature of the interest or interests which required that such purchase or loan be made only after the prior approval of the Administration.

SMALL BUSINESS ADMINISTRATION,
OFFICE OF THE ADMINISTRATOR,
Washington, D.C., October 4, 1963.

HON. WILLIAM PROXMIRE,
*Chairman, Subcommittee on Small Business,
Committee on Banking and Currency,
U.S. Senate,
Washington, D.C.*

DEAR SENATOR PROXMIRE: By letter dated September 6, 1963, you submitted to the Small Business Administration for comment, a proposed amendment to the Small Business Investment Act of 1958, as amended (hereafter called "the act"), covering affiliated transactions on the part of licensed small business investment companies.

We have carefully reviewed the proposed amendment and it is our considered opinion that such amendment would hamper the flexibility necessary for efficient and successful administration of the small business investment company program, since existing legislation confers on the Small Business Administration full authority to regulate in this area and to take whatever action may appear necessary for the furtherance of the purposes of the act.

The development and regulation of the SBIC industry present the Small Business Administration with dynamic and ever-changing problems in administration, the fruitful solution of which requires that SBA have the maximum possible degree of Administrative adaptability. Revision of the act would have the effect of freezing SBA's position with regard to affiliated transactions and of creating limits on the authority of the Small Business Administration in this area which do not now exist. The Small Business Administration is, therefore, opposed to any new legislation on affiliated transactions.

The Small Business Administration clearly recognizes, however, the need for revision of its regulations on affiliated transactions. The attached draft marked "Exhibit A," of proposed regulations in this area, encompasses needed expansion of the purview of section 107.716 of the regulations to cover conflict-of-interest situations not now covered, publication of the criteria utilized by SBA in passing on affiliated transactions, and disclosure of certain information

on transactions approved by SBA under section 107.716. You will note that the proposed regulation is based upon the ideas embodied in your proposed amendment to the act. Adoption by SBA of this proposed regulation offers, in our opinion, the most effective means at this time of dealing with the problem of affiliated transactions while leaving SBA with the freedom necessary to adequately cope with unforeseen abuses in this area.

It is our intention, assuming the foregoing procedure is acceptable to you, to proceed to make effective the proposed regulation by publication in the Federal Register at an early date.

During the course of the hearings you will recall your request that we insert for the record the proposed procedure for publication of our decisions in the affiliated transactions and which I discussed. Exhibits B and C attached hereto set forth this procedure.

Sincerely,

EUGENE P. FOLEY, *Administrator.*

EXHIBIT A

SECTION 107.716 AFFILIATED TRANSACTIONS

(a) Without the prior written approval of SBA a Licensee shall not—

- (1) purchase any security or other property from any affiliated person;
- (2) sell any security or other property to any affiliated person except shares of stock of which the Licensee is the issuer;
- (3) borrow money or other property from any affiliated person;
- (4) lend money or other property to any affiliated person;
- (5) provide consulting and advisory services to any affiliated person;
- (6) participate in any joint enterprise in which any affiliated person is a participant, except that Licensees which are affiliated persons may participate in financing small business concerns of which they are not an affiliated person.

(b) Without the prior written approval of SBA a Licensee shall not enter into any transaction mentioned in subsection (a) of this section with a person who was an affiliated person of the Licensee within six months prior to such transaction.

(c) Without the prior written approval of SBA no Licensee shall purchase equity securities of or make a loan to a small business concern which is controlled by a person or persons who control another Licensee.

(d) A Licensee or any affiliated person thereof shall not borrow money or other property from a small business concern or from any affiliated person of such concern, to which the Licensee has provided equity capital, made a long-term loan, or is providing consulting and advisory services.

(e) A Licensee shall not lend money or property to any person, directly or indirectly, if such person controls, or is under common control with the Licensee.

(f) For the purposes of this section only, any person who owns beneficially, either directly or through one or more controlled companies, 25 per centum or more of the voting securities of a company, shall be presumed to control such company. Any person who does not so own more than 25 per centum of the voting securities of any company shall be presumed not to control such company. Such presumptions may be rebutted.

(g) Nothing contained in this section is intended to preclude a Licensee from permitting an officer, employee, or representative from serving as a Director of a small business concern for the purpose of protecting its investment in such concern, nor is it intended to prevent a Licensee from taking such action, otherwise permissible under these regulations, as may be necessary to protect an investment that is in jeopardy. Moreover, nothing in this section is intended to preclude a Licensee from entering into any otherwise permissible transaction with a small business concern where an affiliation with the Licensee arises solely from the Licensee's having invested in such small business concern or the Licensee's furnishing of consulting or advisory services to such small business concern.

(h) SBA shall not approve any transaction pursuant to subsection (a) of this section, unless it finds that (1) a majority of the Board of Directors of such Licensee has no affiliation with the small business concern; (2) such transaction has received the affirmative approval of such majority; (3) the

general terms upon which such transaction is to be made are not less favorable to such Licensee than those offered by it to other small business concerns, or those negotiated with the small business concern by the Licensee's affiliated person or persons in a transaction covered by subsection (a) (6) of this section; and (4) such transaction is in furtherance of the purposes of the Act.

(i) Whenever a transaction is approved under this section, the Small Business Administration shall promptly notify the Licensee in writing and cause to be published in a monthly bulletin to be issued by the Small Business Administration a summary setting forth the terms of the transaction, the nature of the affiliation requiring the granting of such approval and the application of the criteria set forth in subsection (h) of this section. Within ten days from the entering into of such a transaction, the Licensee shall publish in a newspaper of general circulation, in the locality in which it has its principal place of business, a notice setting forth the terms of the transaction and the nature of the affiliation which required that such transaction required the prior approval of the Small Business Administration.

(j) Any affiliated transaction by a Licensee which is subject to regulation by the Securities and Exchange Commission under the Investment Company Act of 1940, shall be exempt from subsection (i) of this section.

In addition, section 107.12 of the regulations would be amended by the addition thereto of the following definitions.

"Affiliated person" of another person means (a) any person directly or indirectly owning, controlling, or holding with power to vote, 10 per centum or more of the outstanding voting securities of such other person; (b) any person 10 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; (c) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (d) any officer, director, partner, copartner, or close relative of such other person; (e) if such other person is a small business investment company, any investment adviser (as covered by sec. 107.704(d) of these regulations) thereof; and (f) any affiliated person of such a person.

"Close relative" means any lineal ancestor, lineal descendant, spouse, brothers, or sisters (by the whole or half blood); any lineal ancestor, lineal descendant, brother, or sister (by the whole or half blood) of a spouse; first cousins, uncles, aunts, nephews, nieces, (by blood or by marriage); all step relations in the above categories and lineal descendants.

"Control" means the power, directly or indirectly, to exercise a controlling influence over the management or policies of a company, through the ownership of voting securities, by contract or otherwise.

"Joint enterprise" means any transaction or transactions whereby a small business concern receives financing from a Licensee and an affiliated person thereof either simultaneously or at different times.

"Person" means a natural person, a corporation, partnership, pension fund, profit-sharing fund, an association, a joint-stock company, a business trust, and any other organization of whatever nature.

"Voting security" means any security presently entitling the owner or holder thereof to vote for the election of directors of a company.

EXHIBIT B

PROCEDURE ON DISCLOSURE OF AFFILIATED TRANSACTIONS

The procedure for public disclosure of facts on transactions approved under section 107.716 of the regulations under the Small Business Investment Act of 1958, as amended, would encompass publication of basic information about the transaction and about the Small Business Administration's approval of it.

The matters to be disclosed are—

(1) The interrelationships between the small business investment company and the small business concern that caused the transaction to require prior Small Business Administration approval under section 107.716.

(2) The essential terms of the transaction.

(3) The Small Business Administration's criteria and the manner of their application to the transaction.

With regard to disclosure of affiliations, all relationships would be identified with as much precision as possible, i.e., exact titles of officers would be given and the precise amount of stockholdings of 10 or more percent would be disclosed.

As for the terms of the transaction, there would be disclosed, interest rate, maturity, amortization, and security, if any. Where there is an equity investment, the nature of the equity security, the proportion of the small business concern's equity which it represents, and the price of such equity position would be disclosed. Similar disclosure would be made of basic terms of any other transaction falling under section 107.716.

The manner of disclosing the application of the criteria under section 107.716 can best be seen in the attached sample summary marked "Exhibit C." Since the Securities and Exchange Commission will publish a release on each of its actions affecting publicly held small business investment companies, to avoid duplication of effort we would attempt an arrangement between the Small Business Administration and the Securities and Exchange Commission whereby the Securities and Exchange Commission would include, in its order on the transaction, a statement to the effect that the Small Business Administration had approved the transaction under section 107.716.

Publication would be implemented by the issuance of a monthly bulletin by the Small Business Administration which would cover such transactions. In the case of public small business investment companies, the bulletin would simply make reference to the transaction and cite the appropriate Securities and Exchange Commission release. A mailing list for the bulletin would be established by combining present Small Business Administration mailing lists. Anyone who so requests would be placed on the mailing list for the bulletin, but all persons on the list will be required to indicate each year, a desire to continue to receive the bulletin or else their names will be removed from the list. A file of all such summaries would be maintained and available for public inspection. Copies of all or any part of such file could be available to members of the public on request, on payment of an appropriate fee.

EXHIBIT C

SAMPLE SUMMARY ON SECTION 107.716 TRANSACTION

On -----, 1963, a transaction between XYZ, a small business investment company, a Federal licensee under the Small Business Investment Act of 1958, as amended, and the ----- company, a small business concern, was approved by the Small Business Administration, pursuant to section 107.716 of the regulations governing small business investment companies (13 CFR 107.716).

Section 107.716 prohibits a small business investment company from engaging in certain transactions with affiliated persons without the prior written approval of the Small Business Administration.

This investment was brought within the purview of section 107.716 by virtue of the following fact(s) :

Mr. Jones, who is secretary of, and a member of the board of directors of XYZ, is treasurer of, and a member of the board of directors of the ----- company.

This investment consists of the purchase of a convertible debenture of XYZ by the small business investment company for the price of, and in the face amount of \$50,000. The convertible debenture has a maturity of 8 years and bears interest at 8 percent. The debentures are convertible into 15 percent of the equity of the small business concern. The debentures are not secured, and amortization of the principal is to commence in the second year of the life of the debentures.

The general criteria employed by the Small Business Administration in granting or denying approval of investments under section 107.716 are—

(1) A majority of the licensee's directors must have no interest in the proposed transaction, and must have approved it by an affirmative vote.

(2) The terms of the investment must be fair and reasonable.

(3) The investment must serve the purposes of the Small Business Investment Act of 1958, as amended.

All of the directors of the XYZ were informed of the above-mentioned individual's connection with the small business concern, and of the proposed investment in it before the directors of the small business investment company voted on the transaction. The investment was approved by the board of directors of the XYZ in the absence of the member connected with the small business concern.

The Small Business Administration is satisfied that the terms of the investment are fair and reasonable and would not have been materially different in the absence of any affiliation between the small business investment company and the small business concern. Further, the Small Business Administration is satisfied that this amendment serves the purposes of the Small Business Investment Act of 1958, as amended.

Senator PROXMIRE. Our next witness is Mr. Jack Whitney, Securities and Exchange Commission, and we are delighted to have you.

Senator McINTYRE. Mr. Chairman, I thought there was going to be some effort made to secure the writer of this article.

Senator PROXMIRE. There was indeed. I might say we tried hard to get the Wall Street Journal to send their experts up here, and they did a beautiful job in this article. They said the article spoke for itself, and so many people worked on it they probably couldn't fit at the witness table.

Newspapers are always shy.

We are delighted to have you, Mr. Whitney. Go ahead.

You might identify the men who are with you.

STATEMENT OF JACK M. WHITNEY II, COMMISSIONER, SECURITIES AND EXCHANGE COMMISSION; ACCOMPANIED BY EDMUND H. WORTHY, DIRECTOR, DIVISION OF CORPORATION FINANCE; ALLAN F. CONWILL, DIRECTOR, DIVISION OF CORPORATE REGULATION; WALTER P. NORTH, ASSOCIATE GENERAL COUNSEL, OFFICE OF THE GENERAL COUNSEL; ROBERT H. BAGLEY, ASSISTANT DIRECTOR, DIVISION OF CORPORATION FINANCE; GEORGE P. MICHAELY, JR., SPECIAL COUNSEL, OFFICE OF THE GENERAL COUNSEL; AND RICHARD H. BRILL, LEGAL ASSISTANT TO COMMISSIONER WHITNEY

Mr. WHITNEY. Mr. Chairman, Senator Dominick, Senator McIntyre; I am glad to be here today.

On my right is Allan F. Conwill, Director of the Division of Corporate Regulation. As such, he is responsible to the Commission for our regulatory activities under the Investment Company Act of 1940, which involves the SBIC's.

On my immediate left is Mr. Edmund H. Worthy, Director, Division of Corporation Finance, which by contrast deals with our disclosure activities under the Securities Act of 1933 and the Securities Exchange Act of 1934.

On my second left, Mr. Walter P. North, Associate General Counsel. Senator PROXMIRE. What was that name?

Mr. WHITNEY. Walter P. North, Associate General Counsel, and on his left, Mr. Robert Bagley, Assistant Director of the Division of Corporation Finance.

Mr. Chairman, I have a statement here, which I have provided and I propose to read it in large part although I may abbreviate it in spots.

I am here at your invitation to testify on behalf of the Commission with respect to the matters of self-dealing and conflicts of interest in transactions between small business concerns and small business investment companies—SBIC's—which are licensed by the Small Business Administration.

Three proposals have been suggested as possible methods of dealing with these matters. Each of the proposals would be applicable to transactions in which an SBIC makes a loan to, or purchases any equity security of, a small business concern: (1) If an officer or director of the SBIC, or a close relative of such officer or director, is an officer of the small business concern, or owns or controls—directly or indirectly—10 percent or more of the stock of the small business concern; (2) if any person who owns or controls—directly or indirectly—10 percent or more of the stock of the SBIC also owns or controls—directly or indirectly—10 percent or more of the stock of the small business concern, or is a close relative of any such person; or (3) if any person who is an officer or director of the small business concern or owns or controls—directly or indirectly—10 percent or more of the stock of such concern served as an officer or director or owned or controlled—directly or indirectly—10 percent or more of the stock of the SBIC, within 6 months prior to the transaction. The first proposal would impose an outright ban on such transactions; the second would permit such transactions only when prior approval has been obtained from the Small Business Administration in accordance with certain specified standards; and the third would require disclosure of certain of the details of any such transaction by newspaper publication within 30 days following the event.

It is our understanding that the proposals are suggested as possible amendments to the Small Business Investment Act of 1958. As is more fully set forth below, we consider the comprehensive regulatory pattern of the Investment Company Act to be an effective and workable approach for dealing with these problems in transactions affecting publicly held SBIC's.

We would urge that this regulatory pattern be left intact as to such SBIC's and that any legislation be drafted so as to avoid possibly conflicting regulation.

The Commission on which I am privileged to serve is charged with the responsibility of administering the Federal securities laws. Those acts reflect a recognition by the Congress of the need for a broad range of protections for the investing public.

Under the Securities Act of 1933 protections are provided principally through the requirement of full disclosure of pertinent information to persons to whom securities are publicly offered for sale. The Investment Company Act provides protections, in addition to those provided by the Securities Act, which experience had shown were necessary for public investors in companies primarily engaged in the business of investing, reinvesting, and trading in securities.

This grew out of the special study made by the Commission and reported to the Congress for the most part in 1939 and 1940, and it was on the basis of that report that the Congress decided disclosure was not enough in this field.

Now, among other things, the Investment Company Act requires disclosure of financial and investment policies of investment companies, prohibits such companies from changing the nature of their business or their investment policies without the approval of their shareholders, regulates the safekeeping of the companies' assets, places certain restrictions on the composition of the boards of directors of such companies, requires management contracts to be submitted to se-

curities holders for their approval, requires the filing with the Commission and the transmittal to shareholders of periodic reports, requires compliance with the Commission's proxy rules in connection with meetings of shareholders, and places certain limitations on the amount of debt securities which may be issued by investment companies. In particular, in respect of the matters which this committee is now considering, the Investment Company Act includes provisions designed to regulate transactions of affiliated persons affecting investment companies having substantial public stockholder interest.

When the Securities Act was adopted the Congress made a basic policy determination that the national public interest was affected when securities are sold or offered for sale to the public. Again, in adopting the Investment Company Act the Congress made a similar determination that different considerations are applicable to investment companies in which public stockholders are interested than are applicable to investment companies which are private in nature. These policy determinations were not disturbed in 1958 when the Small Business Investment Act was enacted by the 85th Congress. At that time the Congress determined that with certain minor exceptions the provisions of both the Securities Act and the Investment Company Act should apply to SBIC's whose securities are offered or sold to the investing public to the same extent as to investment companies generally. SBIC's in which there is not the requisite public investor interest are not subject to the registration and regulatory provisions of the Federal securities laws. However, all SBIC's must satisfy the requirements of the Small Business Administration in order to be licensed as an SBIC and to qualify for loans of Federal funds to assist them in a program of supplying equity capital to small business concerns.

An SBIC must file a registration statement under the Securities Act only when it proposes to make a public offering of its securities and must register under the Investment Company Act if it makes or proposes to make such a public offering, or if its outstanding securities are beneficially owned by more than 100 persons. As of September 4, 1963, a total of 70 SBIC's were registered with the Commission under the Investment Company Act, all of which had filed registration statements under the Securities Act.

In view of the basic policy underlying the enactment of the Securities Act and the Investment Company Act, that is, the recognition of the distinction between public investor interests and private interests, the Congress might decide that, if legislation is necessary, the pattern of regulation presently applicable to investment companies in which there is public investor interest is not appropriate for SBIC's which do not have a significant number of public shareholders. In any event, we believe that an explanation of our administration of the Securities Act and Investment Company Act should contribute to this subcommittee's consideration of the problems before it.

The provisions of the Investment Company Act relating to conflicts of interest are contained principally in section 21 and section 17 of the act.

Section 21 of the act flatly prohibits an investment company from lending money or property to any person or company who controls or is under common control with the registered investment company.

Senator PROXMIRE. May I ask at this point, what does "lending" mean? Does that include an equity investment or include simply a loan in the usual sense?

Mr. WHITNEY. I believe the term "equity security" in the SBIC sense would include the debt instruments, such as the convertible debenture or the loan accompanied by warrants, but if you had an outright purchase of stock without any debt connection, you would not be under this provision.

Mr. CONWILL. That is correct, the convertible, however, would be.

Mr. WHITNEY. That would be a debt instrument and therefore be evidence of a loan.

Senator PROXMIRE. In other words, if the SBIC should buy outright the equity security from a small business, in which case the owner of the small business was also a director or major stockholder and so forth, qualified clearly as a principal in the SBIC, under this provision of the law at least, it would not be banned?

Mr. WHITNEY. That is correct. It would be caught by the next provision, which is not a flat prohibition.

I would like to refer to that. This is a matter I believe Mr. Parris was commenting on earlier. In considering this section 21, which I have just mentioned, and section 17 which I am now coming to, please bear in mind that there is a distinction to be drawn between a person who controls or is under common control with the SBIC and one who is merely affiliated.

The terms of affiliation are not, of course, as stringent as the term of control, so the prohibition of section 21 refers to a person who is in control or is under common control with the SBIC.

Senator PROXMIRE. How do you define "control"?

Mr. WHITNEY. "Control" is defined in the act as the power to influence the management policies of the SBIC.

Senator PROXMIRE. A director-stockholder who holds 10 percent or more stock?

Mr. WHITNEY. No, sir; there is a statutory presumption that a person who holds 25 percent or more is deemed to be in control, but he may rebut that presumption in a proceeding before us, if he wishes to do so or wishes to attempt to do so. But I mention this because this question of control versus affiliation, which involves usually a 5-percent test, as I will mention in a moment, could be confusing to people.

Senator PROXMIRE. You would assume that a director would be in a position to influence the decision of management?

Mr. WHITNEY. You and I would say he was as a businessman, as a member of the directorate, that is what he was there for, but under the act he would not be in control unless other circumstances supported that.

Now, section 17(a) in general makes unlawful, in the absence of an exemptive order issued by the Commission under section 17(b), transactions with a registered investment company or a company controlled by a registered investment company involving the sale to such company, or the purchase from it, of securities or other property or the borrowing from such company of money or other property, by an affiliated person, promoter or principal underwriter of the registered investment company or by an affiliated person of such affiliated person, promoter, or underwriter.

An affiliated person is defined to include (a) an officer, director, employee, or partner of such other person, (b) a person holding 5 percent or more of the voting securities of the other person, (c) a person 5 percent or more of the securities of which is held by the other person, or (d) a person who directly or indirectly controls or is controlled by or is under common control with the other person.

Senator PROXMIRE. This exemptive order is of the same nature as what the SBA now requires of SBIC's who engage in self-dealing?

Mr. WHITNEY. What you have, sir, is this situation.

In the case of a publicly held SBIC, which is registered with us, at the same time that they would be applying to the SBA for permission under the SBA's regulation 716, they would be applying to us for an exemptive order under section 17(b). The standards in our statute are not the same as the regulation. I am coming to those standards at this point.

Senator PROXMIRE. All right.

Mr. WHITNEY. Section 17(b) of the act provides that the Commission shall, upon application, and after notice and opportunity for public hearing, grant an exemption from the prohibitions of section 17(a) if it finds that (1) the terms of a proposed transaction, including the consideration to be paid, or received, are reasonable and fair and do not involve overreaching on the part of any person concerned, (2) the proposed transaction is consistent with the investment policy of the investment company, and (3) the proposed transaction is consistent with the general purpose of the act.

Senator PROXMIRE. You say nothing about disinterested persons having the power to block—

Mr. WHITNEY. There is nothing in the statute on that subject.

In addition to the provisions of section 17(b), which permit the Commission to exempt individual transactions, the act confers upon the Commission the authority to grant exemptions by rule, regulation or order for certain categories of transactions and persons.

Pursuant to this authority the Commission has adopted rules to exempt from the prohibitions of section 17(a) certain banking transactions made in the ordinary course of business rather than as investments; transactions between the investment company and its wholly owned subsidiaries; consummation of contractual commitments of the investment company where certain conditions are satisfied; and certain pro rata distributions made by the investment company.

As I previously pointed out, under section 17(a) an investment company may not lend money to a portfolio company if the investment company owns 5 percent or more of the portfolio company's stock. As an accommodation to the nature of an SBIC's relationship with its portfolio companies, the Commission adopted a rule permitting investments in and loans to a small business concern by an SBIC notwithstanding SBIC's ownership of 5 percent or more of the voting securities of the small business concern.

Senator PROXMIRE. That means you made a special exception for SBIC's?

Mr. WHITNEY. Generally.

Senator PROXMIRE. Not available to others?

Mr. WHITNEY. In other words, it was recognized that one of the functions of the SBIC was to make equity investments. I think the

record indicates that it was expected they would make rather large investments in any particular small business concern.

The 5-percent rule would therefore have operated as quite a handicap on their ability to do exactly what they were supposed to do.

Senator PROXMIRE. Is this also done because the SBA supervises the self-dealing provision and requires permission before the self-dealing loan is approved?

Mr. WHITNEY. I don't recall that was considered.

Mr. WORTHY?

Mr. WORTHY. As I understand it, Senator Proxmire, I think that at the time that the rule was adopted, that it was taken up and considered with the officials of the SBA.

Senator PROXMIRE. I presume that would be a consideration, after all, if the other Government agency has its own rules, it is particularly subject to SBA supervision, why duplicate it?

Mr. WHITNEY. Correct.

Section 17(d) makes unlawful any transaction in which the investment company, or a company controlled by it, is a joint or joint and several participant with its principal underwriter, or an affiliate of the principal underwriter, or an affiliate of the investment company or an affiliate of such affiliate when entered into in contravention of rules and regulations adopted by the Commission for the purpose of limiting or preventing participation by a registered investment company or a controlled company thereof on a basis different from or less advantageous than that of the affiliated participant.

Pursuant to section 17(d) the Commission has adopted rule 17d-1 which in general prohibits transactions within the scope of section 17(d) of the act unless an application with respect to such transaction has been filed and the Commission has entered an order granting the application.

Rule 17d-1 provides that in passing upon such applications the Commission will consider whether the participation of the investment company or its controlled company in the joint enterprise on the basis proposed is consistent with the provisions, policies, and purposes of the act and the extent to which such participation is on a basis different from or less advantageous than that of other participants.

Senator PROXMIRE. What does that mean?

Mr. WHITNEY. That means that if the investment company and I as an affiliate, are going into a deal together, the investment company's terms are just as good as mine and that I haven't taken advantage of my position to get more favorable terms in the joint venture than I would have gotten absent my relationship.

Senator PROXMIRE. You determine that on the basis of just analyzing a particular company?

Mr. WHITNEY. The particular transaction. We will have a record in which the main thrust is to determine that the transaction bears the earmarks of an arms-length transaction so far as the affiliate and its joint venturer, the investment company, are concerned.

Senator DOMINICK. Mr. Whitney, just commenting on the language here on page 7, you say in here:

Section 17(d) makes unlawful any transaction in which the investment company—

and then you skip down a little—

is an affiliate of the investment company.

What in the world does that mean?

Mr. WHITNEY. Is a joint participant with the affiliate. In the second line, sir, of that paragraph.

Senator DOMINICK. Thank you.

Mr. WHITNEY. I grant you, this is part of our trouble, just to follow the language of the statute.

Section 17(e) of the act provides that no affiliated person of a registered investment company, or affiliate of such affiliated person may receive any compensation for acting as an agent for the investment company, except in the course of such person's business as an underwriter or a securities broker. Section 17(e) also places a specified limitation on the permissible underwriting or brokerage commission.

Thus, as I have outlined here, in summary, section 17 specifies prohibited transactions and the persons who are disqualified from entering into such transactions, sets forth the standards for exemption and provides a mechanism for obtaining such exemption.

In the administration of the act, the staff of the Commission, represented here today by the two heads of the principal divisions concerned, often has informal conferences with managers of, and persons affiliated with, registered investment companies regarding applications under section 17(b) or rule 17d-1. The investment company officials advise the staff of their intentions and the staff expresses its views in light of its experience and applicable administrative precedents as to whether the proposals meet the statutory standards.

These conferences sometimes result in proposals being abandoned without the filing of a formal application, or if a formal application has been filed, either the withdrawal or material modification of the application. Because of these informal procedures, Commission rejection of an application is the exception rather than the rule.

The general technique of informal communication has always been employed in the Commission's administration of the Securities Act of 1933. The few denials of requests for acceleration of registration statements and the small number of stop order and other administrative enforcement proceedings necessarily instituted demonstrate the convenience and workability of the system, both to the agency and to the industry. The practice here described logically follows in the Commission's administration of the Investment Company Act.

Quite apart from the provisions of section 17, the Investment Company Act, the Securities Act and the Securities Exchange Act of 1934 provide for the disclosure of material transactions with affiliated persons. These disclosures arise in three ways: (1) in reports filed with the Commission under the Investment Company Act; (2) in proxy statements filed pursuant to Commission rules and furnished to shareholders; and (3) in registration statements under the Securities Act.

Basically, the disclosure requirements are the same as to each. If the company during its last fiscal year has had a material transaction or if it proposes to have any material transaction in which affiliated persons have a material interest, the transaction and the interest must be disclosed.

Senator PROXMIRE. Disclosed to whom?

Mr. WHITNEY. To the persons receiving one or another of these documents. The proxy statements would go to shareholders of the SBIC, for example. The prospectus would go to the purchaser of stock of the SBIC in a public offering.

The reports to the Commission are a public record and are available in our public reference room.

Senator PROXMIRE. This would be public disclosure in the event the affiliate would be able to get self-approval.

Mr. WHITNEY. Precisely so. As a matter of fact, the proxy statements, quite apart from going to the stockholders in connection with a meeting, are again a part of our public file for anyone else who wants to see them.

The principal item which provides this disclosure, which is common to all of these documents, reads as follows:

Describe briefly, and where practicable state the approximate amount of, any material interest, direct or indirect, of any of the following persons in any material transactions since the beginning of the issuer's last fiscal year, or in any material proposed transactions, to which the issuer or any of its subsidiaries was or is to be a party. Those persons include (3) any director or officer of the issuer; (2) any nominee for election as a director; (3) any security holder (holding 10 percent or more of the issuer's voting securities); (4) any associate of any of the foregoing persons.

Senator PROXMIRE. Do you publicly disclose the amount involved and terms of the investment?

Mr. WHITNEY. Yes, sir.

Senator PROXMIRE. That is a matter of public record.

Mr. WHITNEY. Yes, sir.

Senator PROXMIRE. I imagine the SEC has done this for how long, this goes back to 1940?

Mr. WHITNEY. This is conventional. It arose even prior to the 1940 act, under the 1933 act, in connection with prospectus and subsequently under our proxy rules and, finally, when the Investment Company Act came along, it required similar disclosures filed with us and also required the investment companies to observe the proxy rules that are in the 1934 act.

Senator PROXMIRE. So you have had disclosure experience now for 30 years?

Mr. WHITNEY. Yes, sir.

Senator PROXMIRE. I realize you haven't personally been with them for 30 years—

Mr. WHITNEY. I am beginning to think I feel as though I have.

Senator PROXMIRE. From what you know about the agency and from your own experience, has there been any feeling that this is a competitive disadvantage or that this involves any kind of difficulty from the standpoint of those who have disclosed the information, those who are involved, it handicaps them in any serious or significant way?

Mr. WHITNEY. We don't consider that so. There is this factor to be mentioned, which was not mentioned in my prepared statement, and I should add to it at this point.

Both in the applications for the transactions under the 1940 act, for an exemptive order, and also as a general matter, in the disclosure field, we consider and act upon requests for confidential treatment, but

I don't believe it has been the position of the Commission generally that the competitive factor weighs too heavily in that scale.

Senator PROXMIRE. How common is this confidential treatment? I take it that means there is no disclosure?

Mr. WHITNEY. You would have limitations. You might not disclose the particular aspect which the applicant would consider harmful to it. You might have a great part of the transaction disclosed without a particular—

Senator PROXMIRE. Can you give us an example of what would not be disclosed? You would not disclose the term or relationship of the affiliate? What aspect of this is often or occasionally at least considered to be appropriate to conceal?

Mr. CONWILL. We had a recent application by an investment company, which was not an SBIC, where two affiliates were entering into a contractual transaction which provided for a long-term production contract with respect to a certain mineral.

They requested confidential treatment as to the composition of the mineral that they were taking. The mineral was generic, but the—

Senator PROXMIRE. That would be required to be publicly disclosed anyway?

Mr. CONWILL. We require a lot of information, Mr. Chairman.

Senator PROXMIRE. What I am driving at is this, in your experience is the confidential treatment ever given to the relationship of the affiliate to the lending concern or the terms of the loan, that is, the financial terms, the interest rate, whatever is involved?

Mr. CONWILL. No, sir.

Senator PROXMIRE. It is not; and it is not a problem of confidentiality. You don't get protests saying that if this is disclosed, it is likely to be harmful in some way?

Mr. CONWILL. We hear protests from time to time, Mr. Chairman. We are inclined to dismiss them as not appropriate.

Senator DOMINICK. If I may say for the record on that, every lawyer who is advising his client is told by his client that every bit of information is going to be almost ruinous to his company, and you therefore will have to fight with your own client so you can get something through the SEC.

Otherwise, it doesn't get passed on, and as a matter of fact, it usually is not harmful, but sometimes I suspect that it could be.

Mr. WHITNEY. I can conceive of a situation; I would be surprised if it had arisen under the 1940 act, but we have had cases where under the 1933 act, where confidential treatment of something that was a financing term, that is to say, let's say a lessee of a large piece of equipment, might be getting, for very good business reasons, in an arm's-length transaction, a certain financial benefit in terms of the lease from the manufacturer of that item of equipment, and they would consider that it would be disadvantageous to have that known generally, because for example, the manufacturer might not wish to make those terms generally available. It would not involve the kind of thing you are talking about.

Senator PROXMIRE. The SBIC, which is a financial institution, not a manufacturing institution—

Mr. WHITNEY. I don't conceive this sort of thing would arise there.

Senator PROXMIRE. Very good.

Mr. WHITNEY. As I mentioned, the Investment Company Act extends the proxy regulations to the SBIC's. Rule 20a-3, also supplements the proxy regulations by requiring disclosure of the same information in respect of material transactions in which the investment adviser of an investment company is a party.

Thus, where through inadvertence or lack of familiarity with the provisions of the Investment Company Act, transactions are consummated without obtaining the required Commission order under section 17, the Federal securities acts provide a means for advising shareholders of the transaction and its terms.

Relating the foregoing aspects of the Federal securities laws to the matters under consideration here, we note that they not only impose direct regulation either by forbidding, or by requiring advance Commission approval of certain transactions, but also require disclosure through reports, proxy materials, and registration statements. As a result of our experience in the administration of these acts, we believe that a statutory pattern including both disclosure and direct regulation is an effective and workable approach for dealing with the problem of conflicts of interest in transactions affecting publicly held SBIC's registered under the Investment Company Act. Whether this same pattern should be applied to SBIC's in which there is little, if any, public investor interest but to which Federal funds are advanced is a matter which may involve other considerations and as to which the Commission expresses no opinion.

Senator PROXMIRE. Now, do you see any reasons why small business—and small business does have a much tougher problem in many ways, particularly in financial areas and competitive areas—do you see any reason why small business should be treated somewhat differently here or any way in which we can modify this to protect small business against any possible harm that might come either through prohibition or through disclosure?

Mr. WHITNEY. You could what—modify the proposed legislation?

Senator PROXMIRE. That is correct. You propose, I take it, to apply the Investment Company Act procedures, which I think make an awful lot of sense, for many reasons, to the SBIC's, I take it?

Mr. WHITNEY. We only apply to those. The only jurisdiction is—

Senator PROXMIRE. But your recommendation to this committee, that we follow the Investment Company Act's provision on self-dealing?

Mr. WHITNEY. I am sorry, sir, I think I should make it very clear, we are expressing no position on that point whatever. We are confining our position to the results of our experience with the companies which are publicly held.

Senator PROXMIRE. How about the SBIC's which are publicly held, in which—

Mr. WHITNEY. They are now under our jurisdiction, and these standards apply.

Senator PROXMIRE. You also provide for special treatment for the SBIC's, as I recall. You said that they are subject to, I raised that point when you came to it, they are subject to—

Mr. WHITNEY. That again is a general exception for the SBIC—

Senator PROXMIRE. I remember I raised the point, I said the SBIC's have to go to the SBA for specific consideration and approval in a self-dealing loan. Isn't that another reason, I asked, why they are treated differently or considered exempt from this regulation?

Mr. WHITNEY. Yes, if you are referring back to that point, and, well, I would only say this—

Senator PROXMIRE. I am not saying. I don't think anyone is proposing they should come under SEC; they ought to stay where they are, under SBA, which is competent and does a fine job. I am just asking whether or not, if we do decide to proceed with this legislation, I recognize you don't want to make a recommendation pro or con, if we do decide to proceed, think it would be orderly and sensible to follow the procedures which you now apply.

Mr. WHITNEY. You would certainly expect, or I would suggest that the agency would have the administrative techniques or the authority for that made available to it in terms of the procedures by which they would handle this exemptive power, such as we have.

Senator PROXMIRE. I just want to be sure I understand the situation. Now, you prohibit or provide disclosure, one or the other. Where you may have an exemptive order, it would be a limited exemption from disclosure, and even this is very rare.

Mr. WHITNEY. We would pass on those by an exemptive order.

Senator PROXMIRE. Even where there is an exemptive order, disclosure is required, although there may be, as you have indicated, some limitation on the disclosure involving particular products, never on the terms, and never on the affiliation.

Mr. WHITNEY. That is correct.

Senator PROXMIRE. The SBIC's, which are under Securities and Exchange jurisdiction, for some purposes, however, are—maybe I am wrong, but as I understand your testimony—are exempt from this particular provision.

Mr. WHITNEY. No, sir.

Senator PROXMIRE. Because as you explained it to me, they have to come to the SBA for approval anyway on self-dealing.

Mr. WHITNEY. No, it was just that one provision, which was one rule which is of general application to SBIC's, which, as I referred to on page 7 of my statement, gave a general exception to the SBIC's so that they could have an equity investment in a particular small business concern in an amount greater than 5 percent.

Now, when we were discussing that point, it was recognized, of course, the SBA would still have jurisdiction over the transaction, to the extent it does. And, if it were affiliated transaction, I assume without knowing, that it would be caught by their regulation 716. But, if they didn't have the benefit of that general exemptive rule, they would have to come in for application for exemptive order on the particular transaction.

Senator PROXMIRE. That exemptive rule is a very important rule. That seems to me to exempt a very large portion. Let me read it. [Reads:]

As an accommodation to the nature of an SBIC's relationship with its portfolio companies, the Commission adopted a rule permitting investments in and loans to a small business concern by an SBIC notwithstanding SBIC's ownership of 5 percent or more of the voting securities of the small business concern.

This would be self-dealing for other kinds of institutions, not SBIC's. Others are not exempt. The SBIC's are exempt.

Mr. CONWILL. I wonder if I might make a remark which may be clarifying, Mr. Chairman. There are many types of affiliations and if there are transactions between those affiliates, you must come to our Commission for approval of those transactions.

One affiliation is where the SBIC owns 5 percent or more of the stock of the small business concern, but that is only one. Now, in recognition that would be a very common thing, a very common type of ownership for an SBIC to have, the Commission adopted rule 17a-6 to eliminate the usual requirement for application for an order where that type, but only that type, of affiliation existed.

Senator PROXMIRE. Let me ask you this, then, how often, how many times has SEC granted permission to SBIC's under its jurisdiction to make a self-dealing transaction?

Mr. WHITNEY. Seven times since 1958.

Senator PROXMIRE. Seven times, and do you have any statistics at all on the number of transactions involved under your jurisdiction?

Mr. CONWILL. There have been more instances than that, Mr. Chairman, when SBIC's have come to the staff and informally presented what they proposed to do, prior to the matter being submitted to the Commission, and after discussions with the staff, realizing that they would meet opposition from the staff and realizing that a public hearing would result have declined to proceed with their proposal. I would estimate—

Senator PROXMIRE. I would take maybe 30, 40, 50, or 60 cases in which they have been discouraged and 7 which have been approved; is that about right?

Mr. CONWILL. We don't have statistics on the number of informal approaches to us. I would say that the number would run between 25 and 35.

Senator PROXMIRE. Right. So there have been four or five times as many discouragements as there have been approvals?

Mr. CONWILL. Yes, sir.

Senator PROXMIRE. Now, the other question that I was trying to get—and maybe these statistics aren't available—how many transactions by SBIC's that are under your jurisdiction, how many loans are made. You have the statistics from SBA that it approved 146 self-dealing loans out of 7,000. Now, you have approved seven self-dealing loans out of how many?

If you don't have them, maybe they are not available, maybe you can get it later.

Mr. CONWILL. We would not have them, sir.

Senator PROXMIRE. Does the SBIC have to go to the SEC and SBA to obtain these, those seven; do they also have to go to SBA?

Mr. CONWILL. As I understand regulations of SBA, they have to go to both institutions or agencies.

Senator PROXMIRE. I will yield to the Senator from Colorado, Senator Dominick.

Senator DOMINICK. I just want to make the record clear on only one point, and that is the comments which you have made as to the application of the Investment Act and the other requirements are applicable only to publicly held SBIC's.

Mr. WHITNEY. That is correct.

Senator DOMINICK. And those which are not publicly held, it should be less than 100 shareholders and so on, are not under your

jurisdiction and you are making no recommendations as to what should be done on that; is that correct?

Mr. WHITNEY. That is correct.

Senator DOMINICK. I think you said that there were 70—

Mr. WHITNEY. Seventy companies that are now under the Investment Company Act registered with us, 70 SBIC's. The most we have ever had, was 78 about a year or so ago.

Senator PROXMIRE. May I just ask, the seven approvals are throughout the period of your experience?

Mr. WHITNEY. Since 1958; yes, sir.

Senator DOMINICK. Mr. Chairman, I think this has been helpful information, and I don't think I have anymore questions.

Senator PROXMIRE. Fine, I think it has been helpful, too. I would like to ask one more question. Maybe you would prefer not to answer this or maybe you could answer it informally. Based on your experience in regulating public large investment companies, would you comment on the question of disclosure of certain information to newspapers of general circulation regarding the two factors that we have. You haven't had that kind of disclosure, you have disclosure available in your files, and your disclosure is far more comprehensive than what we are asking.

We ask for disclosure of the affiliation of the person who is receiving the money and disclosure of the terms.

Mr. WHITNEY. I will answer the question, if it is agreeable, strictly as a personal matter. The only experience that I have had with newspaper publication relates to certain kinds of legal notices and so on.

If you will recall, the recent special study of the securities markets leveled some criticisms against this Commission in the area of getting the information which we have in our public files. I grant you they are public. The question is, have we done all we could in making sure that information was readily accessible to those who should be able to use it? And the special study in general concluded we have some more homework to do.

I would say that between that kind of comment, to the extent that it is justified, and my own experience with newspaper publication, I wouldn't attach too much significance to the utility of newspaper publication.

Senator PROXMIRE. At least it is available and people who were alert and looking for it, would have some basis for getting it.

Mr. WHITNEY. That is correct.

Senator PROXMIRE. They wouldn't have to come down to Washington or go to New York to look at the files. It would be an area where SBIC's operated, most of which are reasonably small and so forth.

Fine. Thank you very much. Just one more thing, will you please furnish for the record the applicable SEC laws and regulations for the record of these hearings?

Mr. WHITNEY. Yes, sir.

Senator PROXMIRE. Very good; thank you. Excellent, helpful testimony.

(Mr. Whitney later submitted the following information for inclusion in the record:)

SECURITIES AND EXCHANGE COMMISSION,
Washington D.C., September 23, 1963.

Hon. WILLIAM PROXMIRE,
Chairman, Subcommittee on Small Business,
Committee on Banking and Currency,
U.S. Senate, Washington, D.C.

DEAR SENATOR PROXMIRE: At the hearing relating to small business investment companies on September 5, 1963, you requested that I furnish for the record of the hearing the applicable Federal securities laws and rules and regulations adopted by the Commission. Pursuant to that request, I am sending you herewith pamphlet copies of the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, and a copy of the Commission's rules and regulations adopted under each of those acts. The applicable sections of those statutes and the applicable rules and regulations have been marked in the pamphlet copies and are as follows:

1. Sections 7 and 10 and schedule A of the Securities Act of 1933 and regulation E thereunder;
2. Sections 12, 13, and 14 of the Securities Exchange Act of 1934 and regulations 12B, 13A and 14, schedule 14A and 14B and rules 24b-1, 24b-2 and 24b-3 thereunder; and
3. Sections 17, 20, 21, 24, and 30 of the Investment Company Act of 1940 and rules 17a-1, 17a-2, 17a-3, 17a-4, 17a-5, 17a-6, 17d-1, 17d-2, 17e-1, 20a-1, 20a-2, 20a-3, 30a-1, 30b1-1, 30b2-1 and 30d-1 thereunder.

I am also returning to you a corrected copy of the transcript of my testimony on September 5.

On reading the transcript it appears that the record requires additional clarification concerning the Commission's rule which permits investments in and loans to a small business concern by an SBIC notwithstanding the fact that an SBIC and a small business concern are affiliates because of the ownership by an SBIC of 5 percent or more of the voting securities of a small business concern. The rule permitting such investments is rule 17a-6, adopted under section 17(a) of the Investment Company Act. If an SBIC providing capital to a small business concern acquires 5 percent or more of the voting securities of the small business concern, the SBIC and the small business concern are affiliated persons under one of the definitions of that term in section 2(a)(3) of the Investment Company Act. Accordingly, section 17(a) of the act would prohibit the small business concern from selling any additional stock to, or borrowing any money from, the SBIC unless, after application and a showing that the standards of section 17(b) of the act were met, an exemptive order were obtained from the Commission. In recognition of the fact that an SBIC can ordinarily be expected to make a substantial enough investment in a small business to give rise to affiliation under the act and that an SBIC may provide capital to a small business concern on more than one occasion, the Commission has adopted rule 17a-6. As you will note from the provisions of the rule, it applies only to SBIC's and would permit an SBIC which has provided equity capital to a small business concern to provide additional capital without obtaining a prior Commission order only when the affiliation between the SBIC and the small business concern arises solely by virtue of the ownership by the SBIC of 5 percent or more of the voting securities of the small business concern. The foregoing limitation on the extent of the exemption afforded by this rule is not clear from the transcript of my testimony at the hearing. This exemption would not apply if an officer, director, or principal security holder of the SBIC were also an officer, director, or principal security holder of the small business concern or if the affiliation consisted of anything other than 5 percent or more ownership by the SBIC of voting securities of the small business concern. Any affiliation except such a 5 percent or more ownership would bar transactions of the type here involved except upon advance Commission approval of an application for an exemptive order and a showing that the particular transaction met the standards of section 17(b) of the act.

Sincerely yours,

JACK M. WHITNEY II, *Commissioner.*

[From Securities Act of 1933]

Information Required in Registration Statement

SEC. 7. The registration statement, when relating to a security other than a security issued by a foreign government, or political subdivision thereof, shall contain the information, and be accompanied by the documents specified in Schedule A,¹ and when relating to a security issued by a foreign government, or political subdivision thereof, shall contain the information, and be accompanied by the documents, specified in Schedule B; except that the Commission may by rules or regulations provide that any such information or document need not be included in respect of any class of issuers or securities if it finds that the requirement of such information or document is inapplicable to such class and that disclosure fully adequate for the protection of investors is otherwise required to be included within the registration statement. If any accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, is named as having prepared or certified any part of the registration statement, or is named as having prepared or certified a report or valuation for use in connection with the registration statement, the written consent of such person shall be filed with the registration statement. If any such person is named as having prepared or certified a report or valuation (other than a public official document or statement) which is used in connection with the registration statement, but is not named as having prepared or certified such report or valuation for use in connection with the registration statement, the written consent of such person shall be filed with the registration statement unless the Commission dispenses with such filing as impracticable or as involving undue hardship on the person filing the registration statement. Any such registration statement shall contain such other information, and be accompanied by such other documents, as the Commission may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of investors.

[NOTE: See Appendix, II-A, p. 25, for requirements relating to securities issued under an indenture; see Appendix, II-B, 1, 2, 4, and 5, pp. 25-26, for situations in which alternate materials may be filed or incorporation by reference is permitted; see Appendix II-B, 6, p. 26, for extent of obligation to file supplementary information.]

* * * * *

Information Required in Prospectus

SEC. 10. (a) Except to the extent otherwise permitted or required pursuant to this subsection or subsections (c), (d), or (e)—

(1) a prospectus relating to a security other than a security issued by a foreign government or political subdivision thereof, shall contain the information contained in the registration statement, but it need not include the documents referred to in paragraphs (28) to (32), inclusive, of Schedule A;

(2) a prospectus relating to a security issued by a foreign government or political subdivision thereof shall contain the information contained in the registration statement, but it need not include the documents referred to in paragraphs (13) and (14) of Schedule B;

(3) notwithstanding the provisions of paragraphs (1) and (2) of this subsection (a) when a prospectus is used more than nine months after the effective date of the registration statement, the information contained therein shall be as of a date not more than sixteen months prior to such use, so far as such information is known to the user of such prospectus or can be furnished by such user without unreasonable effort or expense;

(4) there may be omitted from any prospectus any of the information required under this subsection (a) which the Commission may by rules or regulations designate as not being necessary or appropriate in the public interest or for the protection of investors.

(b) In addition to the prospectus permitted or required in subsection (a), the Commission shall by rules or regulations deemed necessary or appropriate in the public interest or for the protection of investors permit the use of a

¹ Section 24(a) of the Investment Company Act of 1940 provides that an investment company registered under that Act may submit copies of the documents which it is required to file under that title in lieu of the registration statement specified in Schedule A of the Securities Act of 1933. [The text of this section is set forth in full in the Appendix, II-B, 2, p. 25.]

prospectus for the purposes of subsection (b)(1) of section 5 which omits in part or summarizes information in the prospectus specified in subsection (a). A prospectus permitted under this subsection shall, except to the extent the Commission by rules or regulations deemed necessary or appropriate in the public interest or for the protection of investors otherwise provides, be filed as part of the registration statement but shall not be deemed a part of such registration statement for the purposes of section 11. The Commission may at any time issue an order preventing or suspending the use of a prospectus permitted under this subsection (b), if it has reason to believe that such prospectus has not been filed (if required to be filed as part of the registration statement) or includes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which such prospectus is or is to be used, not misleading. Upon issuance of an order under this subsection, the Commission shall give notice of the issuance of such order and opportunity for hearing by personal service or the sending of confirmed telegraphic notice. The Commission shall vacate or modify the order at any time for good cause or if such prospectus has been filed or amended in accordance with such order.

(c) Any prospectus shall contain such other information as the Commission may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of investors.

(d) In the exercise of its powers under subsections (a), (b), or (c), the Commission shall have authority to classify prospectuses according to the nature and circumstances of their use or the nature of the security, issue, issuer, or otherwise, and, by rules and regulations and subject to such terms and conditions as it shall specify therein, to prescribe as to each class the form and contents which it may find appropriate and consistent with the public interest and the protection of investors.

(e) The statements or information required to be included in a prospectus by or under authority of subsection (a), (b), (c), or (d), when written, shall be placed in a conspicuous part of the prospectus and, except as otherwise permitted by rules or regulations, in type as large as that used generally in the body of the prospectus.

(f) In any case where a prospectus consists of a radio or television broadcast, copies thereof shall be filed with the Commission under such rules and regulations as it shall prescribe. The Commission may by rules and regulations require the filing with it of forms and prospectuses used in connection with the offer or sale of securities registered under this title.¹

[NOTE: For additional powers of the Commission as to prospectuses of certain investment trust securities see Appendix, II-B, 3, p. 25, and II-D, p. 27.]

¹ Amended by Public No. 577, 83d Cong. Prior to amendment section 10 read as follows: "Sec. 10. (a) A prospectus—

(1) when relating to a security other than a security issued by a foreign government or political subdivision thereof, shall contain the same statements made in the registration statement, but it need not include the documents referred to in paragraphs (28) to (32), inclusive, of Schedule A;

(2) when relating to a security issued by a foreign government or political subdivision thereof shall contain the same statements made in the registration statement, but it need not include the documents referred to in paragraphs (13) and (14) of Schedule B.

(b) Notwithstanding the provisions of subsection (a)—

(1) When a prospectus is used more than thirteen months after the effective date of the registration statement, the information in the statements contained therein shall be as of a date not more than twelve months prior to such use, so far as such information is known to the user of such prospectus or can be furnished by such user without unreasonable effort or expense.

(2) there may be omitted from any prospectus any of the statements required under such subsection (a) which the Commission may by rules or regulations designate as not being necessary or appropriate in the public interest or for the protection of investors.

(3) any prospectus shall contain such other information as the Commission may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of investors.

(4) in the exercise of its powers under paragraphs (2) and (3) of this subsection, the Commission shall have authority to classify prospectuses according to the nature and circumstances of their use, and, by rules and regulations and subject to such terms and conditions as it shall specify therein, to prescribe as to each class the form and contents which it may find appropriate to such use and consistent with the public interest and the protection of investors.

(c) The statements or information required to be included in a prospectus by or under authority of subsection (a) or (b), when written, shall be placed in a conspicuous part of the prospectus in type as large as that used generally in the body of the prospectus.

Schedule A

[NOTE: See Appendix, II-B, 2, p. 25, for requirements with respect to investment companies.]

- (1) The name under which the issuer is doing or intends to do business;
- (2) the name of the State or other sovereign power under which the issuer is organized;
- (3) the location of the issuer's principal business office, and if the issuer is a foreign or territorial person, the name and address of its agent in the United States authorized to receive notice;
- (4) the names and addresses of the directors or persons performing similar functions, and the chief executive, financial and accounting officers, chosen or to be chosen if the issuer be a corporation, association, trust, or other entity; of all partners, if the issuer be a partnership; and of the issuer, if the issuer be an individual; and of the promoters in the case of a business to be formed, or formed within two years prior to the filing of the registration statement;
- (5) the names and addresses of the underwriters;
- (6) the names and addresses of all persons, if any, owning of record or beneficially, if known, more than 10 per centum of any class of stock of the issuer, or more than 10 per centum in the aggregate of the outstanding stock of the issuer as of a date within twenty days prior to the filing of the registration statement;
- (7) the amount of securities of the issuer held by any person specified in paragraphs (4), (5), and (6) of this schedule, as of a date within twenty days prior to the filing of the registration statement, and, if possible, as of one year prior thereto, and the amount of the securities, for which the registration statement is filed, to which such persons have indicated their intention to subscribe;
- (8) the general character of the business actually transacted or to be transacted by the issuer;
- (9) a statement of the capitalization of the issuer, including the authorized and outstanding amounts of its capital stock and the proportion thereof paid up, the number and classes of shares in which such capital stock is divided, par value thereof, or if it has no par value, the stated or assigned value thereof, a description of the respective voting rights, preferences, conversion and exchange rights, rights to dividends, profits, or capital of each class, with respect to each other class, including the retirement and liquidation rights or values thereof;
- (10) a statement of the securities, if any, covered by options outstanding or to be created in connection with the security to be offered, together with the names and addresses of all persons, if any, to be allotted more than 10 per centum in the aggregate of such options;
- (11) the amount of capital stock of each class issued or included in the shares of stock to be offered;
- (12) the amount of the funded debt outstanding and to be created by the security to be offered, with a brief description of the date, maturity, and character of such debt, rate of interest, character of amortization provisions, and the security, if any, therefor. If substitution of any security is permissible, a summarized statement of the conditions under which such substitution is permitted. If substitution is permissible without notice, a specific statement to that effect;
- (13) the specific purposes in detail and the approximate amounts to be devoted to such purposes, so far as determinable, for which the security to be offered is to supply funds, and if the funds are to be raised in part from other sources, the amounts thereof and the sources thereof, shall be stated;
- (14) the remuneration, paid or estimated to be paid, by the issuer or its predecessor, directly or indirectly, during the past year and ensuing year, to (a) the directors or persons performing similar functions, and (b) its officers and other persons, naming them wherever such remuneration exceeded \$25,000 during any such year;

(d) In any case where a prospectus consists of a radio broadcast, copies thereof shall be filed with the Commission under such rules and regulations as it shall prescribe. The Commission may by rules and regulations require the filing with it of forms of prospectuses used in connection with the sale of securities registered under this title."

Prior to amendment by Public No. 291, 73d Cong., Section 10(b)(1) read as follows:

"(1) when a prospectus is used more than thirteen months after the effective date of the registration statement, the information in the statements contained therein shall be as of a date not more than twelve months prior to such use."

* * * * *

(15) the estimated net proceeds to be derived from the security to be offered;

(16) the price at which it is proposed that the security shall be offered to the public or the method by which such price is computed and any variation therefrom at which any portion of such security is proposed to be offered to any persons or classes of persons, other than the underwriters, naming them or specifying the class. A variation in price may be proposed prior to the date of the public offering of the security, but the Commission shall immediately be notified of such variation;

(17) all commissions or discounts paid or to be paid, directly or indirectly, by the issuer to the underwriters in respect of the sale of the security to be offered. Commissions shall include all cash, securities, contracts, or anything else of value, paid, to be set aside, disposed of, or understandings with or for the benefit of any other persons in which any underwriter is interested, made, in connection with the sale of such security. A commission paid or to be paid in connection with the sale of such security by a person in which the issuer has an interest or which is controlled or directed by, or under common control with, the issuer shall be deemed to have been paid by the issuer. Where any such commission is paid the amount of such commission paid to each underwriter shall be stated;

(18) the amount or estimated amounts, itemized in reasonable detail, of expenses, other than commissions specified in paragraph (17) of this schedule, incurred or borne by or for the account of the issuer in connection with the sale of the security to be offered or properly chargeable thereto, including legal, engineering, certification, authentication, and other charges;

(19) the net proceeds derived from any security sold by the issuer during the two years preceding the filing of the registration statement, the price at which such security was offered to the public, and the names of the principal underwriters of such security;

(20) any amount paid within two years preceding the filing of the registration statement or intending to be paid to any promoter and the consideration for any such payment;

(21) the names and addresses of the vendors and the purchase price of any property, or goodwill, acquired or to be acquired, not in the ordinary course of business, which is to be defrayed in whole or in part from the proceeds of the security to be offered, the amount of any commission payable to any person in connection with such acquisition, and the name or names of such person or persons, together with any expense incurred or to be incurred in connection with such acquisition, including the cost of borrowing money to finance such acquisition;

(22) full particulars of the nature and extent of the interest, if any, of every director, principal executive officer, and of every stockholder holding more than 10 per centum of any class of stock or more than 10 per centum in the aggregate of the stock of the issuer, in any property acquired, not in the ordinary course of business of the issuer, within two years preceding the filing of the registration statement or proposed to be acquired at such date;

(23) the names and addresses of counsel who have passed on the legality of the issue;

(24) dates of and parties to, and the general effect concisely stated of every material contract made, not in the ordinary course of business, which contract is to be executed in whole or in part at or after the filing of the registration statement or which contract has been made not more than two years before such filing. Any management contract or contract providing for special bonuses or profit-sharing arrangements, and every material patent or contract for a material patent right, and every contract by or with a public utility company or an affiliate thereof, providing for the giving or receiving of technical or financial advice or service (if such contract may involve a charge to any party thereto at a rate in excess of \$2,500 per year in cash or securities or anything else of value), shall be deemed a material contract;

(25) a balance sheet as of a date not more than ninety days prior to the date of the filing of the registration statement showing all of the assets of the issuer, the nature and cost thereof, whenever determinable, in such detail and in such form as the Commission shall prescribe (with intangible items segregated), including any loan in excess of \$20,000 to any officer, director, stockholder or person directly or indirectly controlling or controlled by the issuer, or person under direct or indirect common control with the issuer. All the liabilities of the issuer in such detail and such form as the Commission shall prescribe, including surplus of the issuer showing how and from what

sources such surplus was created, all as of a date not more than ninety days prior to the filing of the registration statement. If such statement be not certified by an independent public or certified accountant, in addition to the balance sheet required to be submitted under this schedule, a similar detailed balance sheet of the assets and liabilities of the issuer, certified by an independent public or certified accountant, of a date not more than one year prior to the filing of the registration statement, shall be submitted;

(26) a profit and loss statement of the issuer showing earnings and income, the nature and source thereof, and the expenses and fixed charges in such detail and such form as the Commission shall prescribe for the latest fiscal year for which such statement is available and for the two preceding fiscal years, year by year, or, if such issuer has been in actual business for less than three years, then for such time as the issuer has been in actual business, year by year. If the date of the filing of the registration statement is more than six months after the close of the last fiscal year, a statement from such closing date to the latest practicable date. Such statement shall show what the practice of the issuer has been during the three years or lesser period as to the character of the charges, dividends or other distributions made against its various surplus accounts, and as to depreciation, depletion, and maintenance charges, in such detail and form as the Commission shall prescribe, and if stock dividends or avails from the sale of rights have been credited to income, they shall be shown separately with a statement of the basis upon which the credit is computed. Such statement shall also differentiate between any recurring and nonrecurring income and between any investment and operating income. Such statement shall be certified by an independent public or certified accountant;

(27) if the proceeds, or any part of the proceeds, of the security to be issued is to be applied directly or indirectly to the purchase of any business, a profit and loss statement of such business certified by an independent public or certified accountant, meeting the requirements of paragraph (26) of this schedule, for the three preceding fiscal years, together with a balance sheet, similarly certified, of such business, meeting the requirements of paragraph (25) of this schedule of a date not more than ninety days prior to the filing of the registration statement or at the date such business was acquired by the issuer if the business was acquired by the issuer more than ninety days prior to the filing of the registration statement;

(28) a copy of any agreement or agreements (or, if identic agreements are used, the forms thereof) made with any underwriter, including all contracts and agreements referred to in paragraph (17) of this schedule;

(29) a copy of the opinion or opinions of counsel in respect to the legality of the issue, with a translation of such opinion, when necessary, into the English language;

(30) a copy of all material contracts referred to in paragraph (24) of this schedule, but no disclosure shall be required of any portion of any such contract if the Commission determines that disclosure of such portion would impair the value of the contract and would not be necessary for the protection of the investors;

(31) unless previously filed and registered under the provisions of this title, and brought up to date, (a) a copy of its articles of incorporation, with all amendments thereof and of its existing bylaws or instruments corresponding thereto, whatever the name, if the issuer be a corporation; (b) copy of all instruments by which the trust is created or declared, if the issuer is a trust; (c) a copy of its articles of partnership or association and all other papers pertaining to its organization, if the issuer is a partnership, unincorporated association, joint-stock company, or any other form of organization; and

(32) a copy of the underlying agreements or indentures affecting any stock, bonds, or debentures offered or to be offered.

In case of certificates of deposit, voting trust certificates, collateral trust certificates, certificates of interest or shares in unincorporated investment trusts, equipment trust certificates, interim or other receipts for certificates, and like securities, the Commission shall establish rules and regulations requiring the submission of information of a like character applicable to such cases, together with such other information as it may deem appropriate and necessary regarding the character, financial or otherwise, of the actual issuer of the securities and/or the person performing the acts and assuming the duties of depositor or manager.

* * * * *

REGULATION E—EXEMPTION FOR SECURITIES OF SMALL BUSINESS INVESTMENT COMPANIES

Rule 601 Definitions of Terms Used in This Regulation.

As used in this regulation, the following terms shall have the meaning indicated:

Act.—The term "Act" refers to the Securities Act of 1933 unless specifically stated otherwise.

Affiliate.—An "affiliate" of an issuer is a person controlling, controlled by or under common control with such issuer. An individual who controls an issuer is also an affiliate of such issuer.

Notification.—The term "notification" means the notification required by Rule 604.

Offering Circular.—The term "offering circular" means the offering circular required by Rule 605.

State.—A "State" is any State, Territory or insular possession of the United States, or the District of Columbia.

Underwriter.—The term "underwriter" shall have the meaning given in section 2(11) of the Act.

Rule 602 Securities Exempted.

(a) Except as hereinafter provided in this rule, securities issued by any small business investment company which is registered under the Investment Company Act of 1940 shall be exempt from registration under the Securities Act of 1933, subject to the terms and conditions of this regulation. As used in this paragraph, the term "small business investment company" means any company which is licensed as a small business investment company under the Small Business Investment Act of 1958 or which has received the preliminary approval of the Small Business Administration and has been notified by the Administration that it may submit a license application.

(b) No exemption under this regulation shall be available for the securities of any issuer if such issuer or any of its affiliates—

(1) has filed a registration statement which is the subject of any proceeding or examination under section 8 of the Act, or is the subject of any refusal order or stop order entered thereunder within 5 years prior to the filing of the notification;

(2) is subject to pending proceedings under Rule 610 or any similar rule adopted under section 3(b) of the Act, or to an order entered thereunder within 5 years prior to the filing of such notification;

(3) has been convicted within 5 years prior to the filing of such notification of any crime or offense involving the purchase or sale of securities;

(4) is subject to any order, judgment or decree of any court of competent jurisdiction, entered within 5 years prior to the filing of such notification, temporarily or permanently restraining or enjoining such person from engaging in or continuing any conduct or practice in connection with the purchase or sale of securities;

(5) is subject to pending proceedings under section 8(e) of the Investment Company Act of 1940 or to any suspension or revocation order issued thereunder;

(6) is subject to an injunction issued pursuant to section 35(d) of the Investment Company Act of 1940; or

(7) is subject to a United States Post Office fraud order.

(c) No exemption under this regulation shall be available for the securities of any issuer, if any of its directors, officers or principal security holders, any investment adviser or any underwriter of the securities to be offered, or any partner, director or officer of any such investment adviser or underwriter—

(1) has been convicted within 10 years prior to the filing of the notification of any crime or offense involving the purchase or sale of any security or arising out of such person's conduct as an underwriter, broker, dealer or investment adviser;

(2) is temporarily or permanently restrained or enjoined by any court from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security or arising out of such person's conduct as an underwriter, broker, dealer or investment adviser;

(3) is subject to an order of the Commission entered pursuant to section 15(b) or 15A(1) of the Securities Exchange Act of 1934; has been found

by the Commission to be a cause of any such order which is still in effect ; or is subject to an order of the Commission entered pursuant to section 203 (d) or (e) of the Investment Advisers Act of 1940 ;

(4) is suspended or has been expelled from membership in a national securities dealers association or a national securities exchange for conduct inconsistent with just and equitable principles of trade ; or

(5) is subject to a United States Post Office fraud order.

(d) No exemption under this regulation shall be available for the securities of any issuer if any underwriter of such securities, or any director, officer or partner of any such underwriter was, or was named as, an underwriter of any securities—

(1) covered by any registration statement which is the subject of any proceeding or examination under section 8 of the Act, or is the subject of any refusal order or stop order entered thereunder within 5 years prior to the filing of the notification ; or

(2) covered by any filing which is subject to pending proceedings under Rule 610 or any similar rule adopted under section 3 (b) of the Act, or to an order entered thereunder within 5 years prior to the filing of such notification.

(e) Paragraph (b), (c) or (d) shall not apply to the securities of any issuer if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances that the exemption be denied. Any such determination by the Commission shall be without prejudice to any other action by the Commission in any other proceeding or matter with respect to the issuer or any other person.

Rule 603 Amount of Securities Exempted.

(a) The aggregate offering price of all of the following securities of the issuer shall not exceed \$300,000:

(1) all securities presently being offered under this regulation, or specified in the notification as proposed to be so offered ;

(2) all securities previously sold pursuant to an offering under this regulation, commenced within one year prior to the commencement of the proposed offering ; and

(3) all securities sold in violation of section 5(a) of the Act within 1 year prior to the commencement of the proposed offering.

Notwithstanding the foregoing, the aggregate offering price of all securities so offered or sold on behalf of any one person other than the issuer shall not exceed \$100,000, except that this limitation shall not apply if the securities are to be offered on behalf of the estate of a deceased person within 2 years after the death of such person.

(b) The aggregate offering price of securities, which have a determinable market value shall be computed upon the basis of such market value as determined from transactions or quotations on a specified date within 15 days prior to the date of filing the notification, or the offering price to the public, whichever is higher ; provided, that the aggregate gross proceeds actually received from the public shall not exceed the maximum aggregate offering price permitted in the particular case by paragraph (a) above.

(c) In computing the amount of securities which may be offered under this regulation, there need not be included unsold securities the offering of which has been withdrawn with the consent of the Commission by amending the pertinent notification to reduce the amount stated therein as proposed to be offered.

Rule 604 Filing of Notification on Form 1-E.

(a) At least 10 days (Saturdays, Sundays and holidays excluded) prior to the date on which the initial offering of any securities is to be made under this regulation, there shall be filed with the Commission four copies of a notification on Form 1-E. The Commission may, however, in its discretion, authorize the commencement of the offering prior to the expiration of such 10-day period upon a written request for such authorization.

(b) The notification shall be signed by the issuer and each person, other than the issuer, for whose account any of the securities are to be offered. If the notification is signed by any person on behalf of any other person, evidence of authority to sign on behalf of such other person shall be filed with the notification, except where an officer of the issuer signs on behalf of the issuer.

(c) Any amendment to the notification shall be signed in the same manner as the original notification. Four copies of such amendment shall be filed with the Commission at least 10 days prior to any offering of the securities subsequent

to the filing of such amendment, or such shorter period as the Commission, in its discretion, may authorize upon a written request for such authorization.

(d) A notification or any exhibit or other document filed as a part thereof may be withdrawn upon application unless the notification is subject to an order under Rule 610 at the time the application is filed or becomes subject to such an order within 15 days (Saturdays, Sundays and holidays excluded) thereafter; provided, that a notification may not be withdrawn after any of the securities proposed to be offered thereunder have been sold. Any such application shall be signed in the same manner as the notification.

Rule 605 Filing and Use of the Offering Circular.

(a) Except as provided in paragraph (b) of this rule and in Rule 606—

(1) no written offer of securities of any issuer shall be made under this regulation unless an offering circular containing the information specified in Schedule A is concurrently given or has previously been given to the person to whom the offer is made, or has been sent to such person under such circumstances that it would normally have been received by him at or prior to the time of such written offer; and

(2) no securities of such issuer shall be sold under this regulation unless such an offering circular is given to the person to whom the securities were sold, or is sent to such person under such circumstances that it would normally be received by him, with or prior to any confirmation of the sale, or prior to the payment by him of all or any part of the purchase price of the securities, whichever first occurs.

(b) Any written advertisement or other written communication, or any radio or television broadcast, which states from whom an offering circular may be obtained and in addition contains no more than the following information may be published, distributed or broadcast at or after the commencement of the public offering to any person prior to sending or giving such person a copy of such circular:

(1) the name of the issuer of such security;

(2) the title of the security, the amount being offered, and the per-unit offering price to the public; and

(3) the identity of the general type of business of the issuer.

(c) The offering circular may be printed, mimeographed, lithographed or type-written, or prepared by any similar process which will result in clearly legible copies. If printed, it shall be set in roman type at least as large as 10-point modern type, except that financial statements and other statistical or tabular matter may be set in roman type at least as large as 8-point modern type. All type shall be leaded at least 2 points.

(d) If the offering is not completed within nine months from the date of the offering circular, a revised offering circular shall be prepared, filed and used in accordance with these rules as for an original offering circular. In no event shall an offering circular be used which is false or misleading in light of the circumstances then existing.

(e) Four copies of the offering circular required by this rule, which is to be used at the commencement of the offering, shall be filed with the notification at the time such notification is filed and shall be deemed a part thereof. If the offering circular is thereafter revised or amended, four copies of such revised or amended circular shall be filed as an amendment to the notification at least 10 days prior to its use, or such shorter period as the Commission may, in its discretion, authorize upon a written request for such authorization.

Rule 606 Offering Not in Excess of \$50,000.

No offering circular need be filed or used in connection with an offering of securities under this regulation if the aggregate offering price of all securities of the issuer offered or sold without the use of such an offering circular does not exceed \$50,000, computed in accordance with Rule 603, provided the following conditions are met:

(a) There shall be filed as an exhibit to the notification four copies of a statement setting forth the information (other than financial statements) required by Schedule A to be set forth in an offering circular.

(b) No advertisement, article or other communication published in any newspaper, magazine or other periodical and no radio or television broadcast in regard to the offering shall contain more than the following information:

(1) the name of the issuer of such security;

(2) the title of the security, amount offered, and the per-unit offering price to the public;

- (3) the identity of the general type of business of the issuer; and
- (4) by whom orders will be filled or from whom further information may be obtained.

Rule 607 Sales Material to be Filed.

Four copies of each of the following communications prepared or authorized by the issuer or anyone associated with the issuer, any of its affiliates or any principal underwriter for use in connection with the offering of any securities under this regulation shall be filed with the Commission at least 5 days (exclusive of Saturdays, Sundays, and holidays) prior to any use thereof, or such shorter period as the Commission, in its discretion, may authorize:

- (a) every advertisement, article or other communication proposed to be published in any newspaper, magazine or other periodical;
- (b) the script of every radio or television broadcast; and
- (c) every letter, circular or other written communication proposed to be sent, given or otherwise communicated to more than ten persons.

Rule 608 Prohibition of Certain Statements.

No offering circular or other written or oral communication used in connection with any offering under this regulation shall contain any language stating or implying that the Commission has in any way passed upon the merits of, or given approval to, guaranteed or recommended the securities offered or the terms of the offering or has determined that the securities are exempt from registration, or has made any finding that the statements in any such offering circular or other communication are accurate or complete.

Rule 609 Reports of Sales Hereunder.

Within 30 days after the end of each 6-month period following the date of the original offering circular, or of the statement required by Rule 606, the issuer or other persons for whose account the securities are offered shall file with the Commission four copies of a report on Form 2-E containing the information called for by that form. A final report shall be made upon completion or termination of the offering and may be made prior to the end of the 6-month period in which the last sale is made.

Rule 610 Suspension of Exemption.

(a) The Commission may, at any time after the filing of a notification, enter an order temporarily suspending the exemption, if it has reason to believe that—

- (1) no exemption is available under this regulation for the securities purported to be offered hereunder or any of the terms or conditions of this regulation have not been complied with, including failure to file any report as required by Rule 609;
- (2) the notification, the offering circular or any other sales literature contains any untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading;
- (3) the offering is being made or would be made in violation of section 17 of the Act;
- (4) any event has occurred after the filing of the notification which would have rendered the exemption hereunder unavailable if it has occurred prior to such filing;
- (5) any person specified in paragraph (b) of Rule 602 has been indicted for any crime or offense of the character specified in subparagraph (3) thereof, or any proceeding has been initiated for the purpose of enjoining any such person from engaging in or continuing any conduct or practice of the character specified in subparagraph (4) of such paragraph;
- (6) any person specified in paragraph (c) of Rule 602 has been indicted for any crime or offense of the character specified in subparagraph (1) thereof, or any proceeding has been initiated for the purpose of enjoining any such person from engaging in or continuing any conduct or practice of the character specified in subparagraph (2) of such paragraph; or
- (7) the issuer or any officer, director or underwriter has failed to cooperate, or has obstructed or refused to permit the making of an investigation by the Commission in connection with any offering made or proposed to be made hereunder.

(b) Upon the entry of an order under paragraph (a) of this rule, the Commission will promptly give notice to the persons on whose behalf the notification was filed (i) that such order has been entered, together with a brief statement

of the reasons for the entry of the order, and (ii) that the Commission, upon receipt of a written request within 30 days after the entry of such order, will, within 20 days after the receipt of such request, set the matter down for hearing at a place to be designated by the Commission. If no hearing is requested and none is ordered by the Commission, the order shall become permanent on the thirtieth day after its entry and shall remain in effect unless or until it is modified or vacated by the Commission. Where a hearing is requested or is ordered by the Commission, the Commission will, after notice of an opportunity for such hearing, either vacate the order or enter an order permanently suspending the exemption.

(c) The Commission may at any time after notice of and opportunity for hearing, enter an order permanently suspending the exemption for any reason upon which it could have entered a temporary suspension order under paragraph (a) of this rule. Any such order shall remain in effect until vacated by the Commission.

(d) All notices required by this rule shall be given to the person or persons on whose behalf the notification was filed by personal service, registered mail or confirmed telegraphic notice at the addresses of such persons given in the notification.

SCHEDULE A—CONTENTS OF OFFERING CIRCULAR

The offering circular required by Rule 605 shall contain the following information:

1. The following statement shall be set forth on the outside front cover page of the offering circular in capital letters in type as large as that used generally in the body of the circular:

THESE SECURITIES ARE OFFERED PURSUANT TO AN EXEMPTION FROM REGISTRATION WITH THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION. THE COMMISSION DOES NOT PASS UPON THE MERITS OF, OR APPROVE, GUARANTEE OR RECOMMEND, ANY SECURITIES NOR DOES IT PASS UPON THE ACCURACY OR COMPLETENESS OF ANY OFFERING CIRCULAR OR OTHER SELLING LITERATURE.

2. State the exact name and address of the issuer, the name of the State or other jurisdiction under the laws of which it was incorporated and the date of its incorporation.

3. (a) Give the following information, in the tabular form indicated, on the outside front cover page of the offering circular on a per-share or other unit basis.

Offering price to public	Underwriting discounts or commissions	Proceeds to issuer or other persons
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(b) If any of the securities are to be offered for the account of any person other than the issuer, give the name and address of each such security holder, the total amount he owns and the amount to be offered hereunder for his account.

4. (a) State the amount of securities to be offered pursuant to this regulation, the aggregate offering price to the public, the aggregate underwriting discounts or commissions, the amount of expenses of the issuer and the amount of expenses of the underwriters to be borne by the issuer, and the aggregate proceeds to the issuer or security holders for whose account the securities are to be offered.

(b) If the securities are not to be offered for cash, state the basis upon which the offering is to be made.

5. Describe briefly the method by which the securities are to be offered and if the offering is to be made by or through underwriters, the name and address of each underwriter and the amount of the participation of each such underwriter, indicating the nature of any material relationship between the issuer and such underwriter.

6. Furnish a reasonably itemized statement of the purposes for which the net cash proceeds to the issuer from the sale of the securities are to be used and the amount to be used for each such purpose, indicating in what order of priority the proceeds will be used for the respective purposes. If the issuer has not yet obtained a license from the Small Business Administration, state whether the funds paid in by investors for the securities to be offered will be returned to them in the event such license is not obtained and describe the arrangements made to assure such return.

7. Give a brief description of the securities to be offered pursuant to this regulation. Include the following information:

(a) In the case of shares, the par or stated value, if any; the rate of dividends, if fixed, and whether cumulative or noncumulative; a brief indication of the preference, if any; and if convertible, the conversion rate.

(b) In the case of debt securities, the rate of interest; the date of maturity, or if the issue matures serially, a brief indication of the serial maturities, such as "maturing serially from 1965 to 1975"; if the payment of principal or interest is contingent, an appropriate indication of such contingency; a brief indication of the priority of the issue; and if convertible, the conversion rate.

(c) In the case of any other kind of securities, appropriate information of a comparable character.

8. State whether the issuer is a closed-end or open-end investment company, and whether it proposes to operate as a diversified or nondiversified investment company.

Instruction.—The issuer may reserve freedom of action to change from a non-diversified to a diversified investment company.

9. Furnish the information which would be required by Items 2 and 3 of Form N-5 if a registration statement on that form were currently being filed.

10. (a) Give the full names and complete resident addresses of all directors, officers and members of the advisory board of the issuer, any investment adviser of the issuer and any persons who own of record or are known to own beneficially more than 10 percent of any class of securities of the issuer, other than the Small Business Administration.

(b) State the aggregate annual remuneration of all directors and officers of the issuer as a group and the annual remuneration of each of the three highest-paid officers of the issuer.

(c) Describe all direct and indirect interests (by security holdings or otherwise) of each person named in answer to (a) above: (i) in the issuer and (ii) in any material transactions within the past 2 years or in any material proposed transactions to which the issuer was or is to be a party. Include the cost to such persons of any assets or services for which any payment by or for the account of the issuer has been or is to be made.

11. Furnish appropriate financial statements of the issuer as required below. Such statements shall be prepared in accordance with generally accepted accounting principles and practices but need not be certified.

(a) A balance sheet as of a date within 90 days prior to the date of filing the notification with the Commission.

(b) A profit and loss or income statement for each of the last 3 fiscal years and for any subsequent period up to the date of the balance sheet furnished pursuant to (a) above.

* * * * *

[From Securities Exchange Act of 1934]

Registration Requirements for Securities

SECTION 12. (a) It shall be unlawful for any member, broker, or dealer to effect any transaction in any security (other than an exempted security) on a national securities exchange unless a registration is effective as to such security for such exchange in accordance with the provisions of this title and the rules and regulations thereunder.

(b) A security may be registered on a national securities exchange by the issuer filing an application with the exchange (and filing with the Commission such duplicate originals thereof as the Commission may require), which application shall contain—

(1) Such information, in such detail, as to the issuer and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, the issuer, and any guarantor of the security as to principal or interest or both, as the Commission may by rules and regulations require, as necessary or appropriate in the public interest or for the protection of investors, in respect of the following:

(A) the organization, financial structure and nature of the business;

(B) the terms, position, rights, and privileges of the different classes of securities outstanding;

(C) the terms on which their securities are to be, and during the preceding three years have been, offered to the public or otherwise;

(D) the directors, officers, and underwriters, and each security holder of record holding more than 10 per centum of any class of any equity security of the issuer (other than an exempted security), their remuneration and their interests in the securities of, and their material contracts with, the issuer and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, the issuer;

(E) remuneration to others than directors and officers exceeding \$20,000 per annum;

(F) bonus and profit-sharing arrangements;

(G) management and service contracts;

(H) options existing or to be created in respect of their securities;

(I) balance sheets for not more than the three preceding fiscal years, certified if required by the rules and regulations of the Commission by independent public accountants;

(J) profit and loss statements for not more than the three preceding fiscal years, certified if required by the rules and regulations of the Commission by independent public accountants; and

(K) any further financial statements which the Commission may deem necessary or appropriate for the protection of investors.

(2) Such copies of articles of incorporation, bylaws, trust indentures, or corresponding documents by whatever name known, underwriting arrangements, and other similar documents of, and voting trust agreements with respect to, the issuer and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, the issuer as the Commission may require as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security.

(c) If in the judgment of the Commission any information required under subsection (b) is inapplicable to any specified class or classes of issuers, the Commission shall require in lieu thereof the submission of such other information of comparable character as it may deem applicable to such class of issuers.

(d) If the exchange authorities certify to the Commission that the security has been approved by the exchange for listing and registration, the registration shall become effective thirty days after the receipt of such certification by the Commission or within such shorter period of time as the Commission may determine. A security registered with a national securities exchange may be withdrawn or stricken from listing and registration in accordance with the rules of the exchange and, upon such terms as the Commission may deem necessary to impose for the protection of investors, upon application by the issuer or the exchange to the Commission; whereupon the issuer shall be relieved from further compliance with the provisions of this section and section 13 of this title and any rules or regulations under such sections as to the securities so withdrawn or stricken. An unissued security may be registered only in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.²

(e) Notwithstanding the foregoing provisions of this section, the Commission may by such rules and regulations as it deems necessary or appropriate in the public interest or for the protection of investors permit securities listed on any exchange at the time the registration of such exchange as a national securities exchange becomes effective, to be registered for a period ending not later than July 1, 1935, without complying with the provisions of this section.

(f) Notwithstanding the foregoing provisions of this section, any national securities exchange, upon application to and approval of such application by the Commission and subject to the terms and conditions hereinafter set forth, (1) may continue unlisted trading privileges to which a security had been admitted on such exchange prior to March 1, 1934; or (2) may extend unlisted trading privileges to any security duly listed and registered on any other national securities exchange, but such unlisted trading privileges shall continue in

²Public No. 577, 83d Cong., approved Aug. 10, 1954, (68 Stat. 686), and effective 60 days after the date of its enactment, repealed the last sentence of paragraph (d) of Section 12 of this title as originally enacted, which sentence read as follows:

"Such rules and regulations shall limit the registration of an unissued security to cases where such security is a right or the subject of a right to subscribe or otherwise acquire such security granted to holders of a previously registered security and where the primary purpose of such registration is to distribute such unissued security to such holders."

effect only so long as such security shall remain listed and registered on any other national securities exchange;³ or (3) may extend unlisted trading privileges to any security in respect of which there is available from a registration statement and periodic reports or other data filed pursuant to rules or regulations prescribed by the Commission under this title or the Securities Act of 1933, as amended, information substantially equivalent to that available pursuant to rules or regulations of the Commission in respect of a security duly listed and registered on a national securities exchange, but such unlisted trading privileges shall continue in effect only so long as such a registration statement remains effective and such periodic reports or other data continue to be so filed.⁴

No application pursuant to this subsection shall be approved unless the Commission finds that the continuation or extension of unlisted trading privileges pursuant to such application is necessary or appropriate in the public interest or for the protection of investors. No application to extend unlisted trading privileges to any security pursuant to clause (2) or (3) of this subsection shall be approved except after appropriate notice and opportunity for hearing. No application to extend unlisted trading privileges to any security pursuant to clause (2) or (3) of this subsection shall be approved unless the applicant exchange shall establish to the satisfaction of the Commission that there exists in the vicinity of such exchange sufficiently widespread public distribution of such security and sufficient public trading activity therein to render the extension of unlisted trading privileges on such exchange thereto necessary or appropriate in the public interest or for the protection of investors. No application to extend unlisted trading privileges to any security pursuant to clause (3) of this subsection shall be approved except upon such terms and conditions as will subject the issuer thereof, the officers and directors of such issuer, and every beneficial owner of more than 10 per centum of such security to duties substantially equivalent to the duties which would arise pursuant to this title if such security were duly listed and registered on a national securities exchange; except that such terms and conditions need not be imposed in any case or class of cases in which it shall appear to the Commission that the public interest and the protection of investors would nevertheless best be served by such extension of unlisted trading privileges. In the publication or making available for publication by any national securities exchange, or by any person directly or indirectly controlled by such exchange, of quotations or transactions in securities made or effected upon such exchange, such exchange or controlled person shall clearly differentiate between quotations or transactions in listed securities, and quotations or transactions in securities for which unlisted trading privileges on such exchange have been continued or extended pursuant to this subsection. In the publication or making available for publication of such quotations or transactions otherwise than by ticker, such exchange or controlled person shall group under separate headings (A) quotations or transactions in listed securities, and (B) quotations or transactions in securities for which unlisted trading privileges on such exchange has been continued or extended pursuant to this subsection.

The Commission shall by rules and regulations suspend unlisted trading privileges in whole or in part for any or all classes of securities for a period not exceeding twelve months, if it deems such suspension necessary or appropriate in the public interest or for the protection of investors or to prevent evasion of the purposes of this title.

Unlisted trading privileges continued for any security pursuant to clause (1) of this subsection shall be terminated by order, after appropriate notice and opportunity for hearing, if it appears at any time that such security has been withdrawn from listing on any exchange by the issuer thereof, unless it shall be established to the satisfaction of the Commission that such delisting was not designed to evade the purposes of this title or unless it shall appear to the Commission that, notwithstanding any such purpose of evasion, the continuation of such unlisted trading privileges is nevertheless necessary or appropriate in the public interest or for the protection of investors. On the application of the issuer of any security for which unlisted trading privileges on any exchange have been continued or extended pursuant to this subsection, or of any broker or dealer who makes or creates a market for such security, or of any other person having a bona fide interest in the question of termination or suspension of such unlisted

³ By sec. 12 of Public No. 621, 74th Cong., approved May 27, 1936, (49 Stat. 1380), the provisions of this clause did not become effective until 90 days after May 27, 1936.

⁴ By sec. 12 of Public No. 621, 74th Cong., (49 Stat. 1380), the provisions of this clause did not become effective until 6 months after May 27, 1936.

trading privileges, or on its own motion, the Commission shall by order terminate, or suspend for a period not exceeding twelve months, such unlisted trading privileges for such security if the Commission finds, after appropriate notice and opportunity for hearing, that by reason of inadequate public distribution of such security in the vicinity of said exchange, or by reason of inadequate public trading activity or of the character of trading therein on said exchange, such termination or suspension is necessary or appropriate in the public interest or for the protection of investors.

In any proceeding under this subsection in which appropriate notice and opportunity for hearing are required, notice of not less than ten days to the applicant in such proceeding, to the issuer of the security involved, to the exchange which is seeking to continue or extend or has continued or extended unlisted trading privileges for such security, and to the exchange, if any, on which such security is listed and registered, shall be deemed adequate notice, and any broker or dealer who makes or creates a market for such security, and any other person having a bona fide interest in such proceeding, shall upon application be entitled to be heard.

Any security for which unlisted trading privileges are continued or extended pursuant to this subsection shall be deemed to be registered on a national securities exchange within the meaning of this title. The powers and duties of the Commission under subsection (b) of section 19 of this title shall be applicable to the rules of an exchange in respect of any such security. The Commission may, by such rules and regulations as it deems necessary or appropriate in the public interest or for the protection of investors, either unconditionally or upon specified terms and conditions, or for stated periods, exempt such securities from the operation of any provision of section 13, 14, or 16 of this title.⁵

Periodical and Other Reports

SECTION 13. (a) Every issuer of a security registered on a national securities exchange shall file the information, documents, and reports below specified with the exchange (and shall file with the Commission such duplicate originals thereof as the Commission may require), in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security—

(1) Such information and documents as the Commission may require to keep reasonably current the information and documents filed pursuant to section 12.

(2) Such annual reports, certified if required by the rules and regulations of the Commission by independent public accountants, and such quarterly reports, as the Commission may prescribe.

(b) The Commission may prescribe, in regard to reports made pursuant to this title, the form or forms in which the required information shall be set forth, the items or details to be shown in the balance sheet and the earning statement, and the methods to be followed in the preparation of reports, in the appraisal or valuation of assets and liabilities, in the determination of

⁵Attention is directed to sec. 2 of Public No. 621, 74th Cong., (49 Stat. 1377) which reads:

SEC. 2. Any application to continue unlisted trading privileges for any security heretofore filed by any exchange and approved by the Commission pursuant to clause (1) of subsection (f) of section 12 of the Securities Exchange Act of 1934 and rules and regulations thereunder shall be deemed to have been filed and approved pursuant to clause (1) of said subsection (f) as amended by section 1 of this act.

Public No. 621 amended sec. 12(f). As originally enacted, the subsection read as follows:

(f) The Commission is directed to make a study of trading in unlisted securities upon exchanges and to report the results of its study and its recommendations to Congress on or before January 3, 1936. Notwithstanding the foregoing provisions of this section, the Commission may, by such rules and regulations as it deems necessary or appropriate for the protection of investors, prescribe terms and conditions under which, upon the application of any national securities exchange, such exchange (1) may continue until June 1, 1936, unlisted trading privileges to which a security had been admitted on such exchange prior to March 1, 1934, and for such purpose exempt such security and the issuer thereof from the provisions of this section and sections 13 and 16, or (2) may extend until July 1, 1935, unlisted trading privilege to any security registered on any other national securities exchange which security was listed on such other exchange on March 1, 1934. A security for which unlisted trading privileges are so continued shall be considered a "security registered on a national securities exchange" within the meaning of this title. The rules and regulations of the Commission relating to such unlisted trading privileges for securities shall require that quotations of transactions upon any national securities exchange shall clearly indicate the difference between fully listed securities and securities admitted to unlisted trading privileges only.

depreciation and depletion, in the differentiation of recurring and nonrecurring income, in the differentiation of investment and operating income, and in the preparation, where the Commission deems it necessary or desirable, of separate and/or consolidated balance sheets or income accounts of any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer; but in the case of the reports of any person whose methods of accounting are prescribed under the provisions of any law of the United States, or any rule or regulation thereunder, the rules and regulations of the Commission with respect to reports shall not be inconsistent with the requirements imposed by such law or rule or regulation in respect of the same subject matter, and, in the case of carriers subject to the provisions of section 20 of the Interstate Commerce Act, as amended, or carriers required pursuant to any other Act of Congress to make reports of the same general character as those required under such section 20, shall permit such carriers to file with the Commission and the exchange duplicate copies of the reports and other documents filed with the Interstate Commerce Commission, or with the governmental authority administering such other Act of Congress, in lieu of the reports, information and documents required under this section and section 12 in respect of the same subject matter.

(c) If in the judgment of the Commission any report required under subsection (a) is inapplicable to any specified class or classes of issuers, the Commission shall require in lieu thereof of the submission of such reports of comparable character as it may deem applicable to such class or classes of issuers.

Proxies

SECTION 14. (a) It shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of any national securities exchange or otherwise to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered on any national securities exchange in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) It shall be unlawful for any member of a national securities exchange or any broker or dealer who transacts a business in securities through the medium of any such member to give a proxy, consent, or authorization in respect of any security registered on a national securities exchange and carried for the account of a customer in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * * * *

REGULATION 12B. APPLICATIONS AND REPORTS

Article 1. General

Rule 12b-1. Scope of Regulation.

The rules contained in this regulation shall govern all applications for registrations pursuant to section 12 of the Act and reports pursuant to sections 13 and 15(d) of the Act, including all amendments to such applications and reports, except that any provision in a form covering the same subject matter as any such rule shall be controlling.

Rule 12b-2. Definitions.

Unless the context otherwise requires, the following terms, when used in the rules contained in this regulation or in Regulation 13A or 15D or in the forms for applications and reports pursuant to section 12, 13, or 15(d) of the Act, shall have the respective meanings indicated in this rule:

Affiliate.—An "affiliate" of, or a person "affiliated" with, a specified person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.

Amount.—The term "amount," when used in regard to securities, means the principal amount if relating to evidences of indebtedness, the number of shares if relating to shares, and the number of units if relating to any other kind of security.

Associate.—The term "associate" used to indicate a relationship with any person, means (1) any corporation or organization (other than the registrant or a majority-owned subsidiary of the registrant) of which such person is an officer or partner or is, directly or indirectly, the beneficial owner of 10 percent or more of any class of equity securities, (2) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity, and (3) any relative or spouse of such person, or any relative of such spouse, who has the same home as such person or who is a director or officer of the registrant or any of its parents or subsidiaries.

Certified.—The term "certified," when used in regard to financial statements, means certified by an independent public or independent certified public accountant or accountants.

Charter.—The term "charter" includes articles of incorporation, declarations of trust, articles of association or partnership, or any similar instrument, as amended, effecting (either with or without filing with any governmental agency) the organization or creation of an incorporated or unincorporated person.

Control.—The term "control" (including the terms "controlling," "controlled by" and "under common control with") means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.

Employee.—The term "employee" does not include a director, trustee, or officer.

Fiscal year.—The term "fiscal year" means the annual accounting period or, if no closing date has been adopted, the calendar year ending on December 31.

Majority-owned subsidiary.—The term "majority-owned subsidiary" means a subsidiary more than fifty percent of whose outstanding securities representing the right, other than as affected by events of default, to vote for the election of directors, is owned by the subsidiary's parent and/or one or more of the parent's other majority-owned subsidiaries.

Material.—The term "material," when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters as to which an average prudent investor ought reasonably to be informed before buying or selling the security registered.

Parent.—A "parent" of a specified person is an affiliate controlling such person directly, or indirectly through one or more intermediaries.

Predecessor.—The term "predecessor" means a person the major portion of the business and assets of which another person acquired in a single succession or in a series of related successions in each of which the acquiring person acquired the major portion of the business and assets of the acquired person.

Previously filed or reported.—The terms "previously filed" and "previously reported" mean previously filed with, or reported in, an application under section 12, a report under section 13 or 15(d), a definitive proxy statement under section 14 of the Act, or a registration statement under the Securities Act of 1933; provided, that information contained in a report under section 15(d) of the Act or in a registration statement under the Securities Act of 1933 shall be deemed to have been previously filed with, or reported to, an exchange only if such report or registration statement is filed with such exchange.

Principal underwriter.—The term "principal underwriter" means an underwriter in privity of contract with the issuer of the securities as to which he is underwriter.

Promoter.—The term "promoter" includes—

(a) Any person who, acting alone or in conjunction with one or more other persons, directly or indirectly takes initiative in founding and organizing the business or enterprise of an issuer.

(b) Any person who, in connection with the founding and organizing of the business or enterprise of an issuer, directly or indirectly receives in consideration of services or property or both services and property 10 percent or more of any class of securities of the issuer or 10 percent or more of the proceeds from the sale of any class of such securities. However, a person who receives such securities or proceeds either solely as underwriting commissions or solely in consideration of property shall not be deemed a promoter within the meaning of this paragraph if such person does not otherwise take part in founding and organizing the enterprise.

Prospectus.—Unless otherwise specified or the context otherwise requires, the term "prospectus" means a prospectus meeting the requirements of section 10(a) of the Securities Act of 1933 as amended.

Registrant.—The term “registrant” means an issuer of securities with respect to which an application or a report is being filed.

Share.—The term “share” means a share of stock in a corporation or unit of interest in an unincorporated person.

Significant subsidiary.—The term “significant subsidiary” means a subsidiary meeting any one of the following conditions:

(a) The assets of the subsidiary, or the investments in and advances to the subsidiary by its parent and the parent's other subsidiaries, if any, exceed 15 percent of the assets of the parent and its subsidiaries on a consolidated basis.

(b) The sales and operating revenues of the subsidiary exceed 15 percent of the sales and operating revenues of its parent and the parent's subsidiaries on a consolidated basis.

(c) The subsidiary is the parent of one or more subsidiaries and, together with such subsidiaries would, if considered in the aggregate, constitute a significant subsidiary.

Subsidiary.—A “subsidiary” of a specified person is an affiliate controlled by such person directly, or indirectly through one or more intermediaries. (See also “majority-owned subsidiary”, “significant subsidiary”, and “totally-held subsidiary.”)

Succession.—The term “succession” means the direct acquisition of the assets comprising a going business, whether by merger, consolidation, purchase, or other direct transfer. The term does not include the acquisition of control of a business unless followed by the direct acquisition of its assets. The term “succeed” and “successor” have meanings correlative to the foregoing.

Totally-held subsidiary.—The term “totally-held subsidiary” means a subsidiary (a) substantially all of whose outstanding securities are owned by its parent and/or the parent's other totally-held subsidiaries, and (b) which is not indebted to any person other than its parent and/or the parent's totally-held subsidiaries in an amount which is material in relation to the particular subsidiary, excepting indebtedness incurred in the ordinary course of business which is not overdue and which matures within one year from the date of its creation, whether evidenced by securities or not.

Voting securities.—The term “voting securities” means securities the holders of which are presently entitled to vote for the election of directors.

Wholly-owned subsidiary.—The term “wholly-owned subsidiary” means a subsidiary substantially all of whose outstanding voting securities are owned by its parent and/or the parent's other wholly-owned subsidiaries.

Rule 12b-3. Title of Securities.

Wherever the title of securities is required to be stated there shall be given such information as will indicate the type and general character of the securities, including the following:

(a) In the case of shares, the par or stated value, if any; the rate of dividends, if fixed, and whether cumulative or non-cumulative; a brief indication of the preference, if any; and if convertible, a statement to that effect.

(b) In the case of funded debt, the rate of interest; the date of maturity, or if the issue matures serially, a brief indication of the serial maturities, such as “maturing serially from 1950 to 1960”; if the payment of principal or interest is contingent, an appropriate indication of such contingency; a brief indication of the priority of the issue; and if convertible, a statement to that effect.

(c) In the case of any other kind of security, appropriate information of comparable character.

Rule 12b-4. Interpretation of Requirements.

Unless the context clearly shows otherwise—

(a) The forms require information only as to the registrant.

(b) Whenever any fixed period of time in the past is indicated, such period shall be computed from the date of filing.

(c) Whenever words relate to the future, they have reference solely to present intention.

(d) Any words indicating the holder of a position or office include persons, by whatever titles designated, whose duties are those ordinarily performed by holders of such positions or offices.

Rule 12b-5. Determination of Affiliates of Banks.

In determining whether a person is an “affiliate” or “parent” of a bank or whether a bank is a “subsidiary” or “majority-owned subsidiary” of a person, within the meaning of those terms as defined in Rule 12b-2, voting securities of the bank held by a corporation all of the stock of which is directly owned by the United States Government shall not be taken into consideration.

Article 2. Formal Requirements

Rule 12b-10. Requirements as to Proper Form.

Every application or report shall be on the form prescribed therefor by the Commission, as in effect on the date of filing. Any application or report shall be deemed to be filed on the proper form unless objection to the form is made by the Commission within thirty days after the date of filing.

Rule 12b-11. Number of Copies—Signatures—Binding.

(a) Except as provided in a particular form, three complete copies of each application or report, including exhibits and all other papers and documents filed as a part thereof, shall be filed with the Commission. At least one complete copy of each application shall be filed with each exchange on which the securities covered thereby are being registered. At least one complete copy of each report under section 13 of the Act shall be filed with each exchange on which the registrant has securities listed and registered.

(b) At least one copy of the application or report filed with the Commission and one copy thereof filed with each exchange shall be manually signed in the manner prescribed by the appropriate form. If the application or report is typewritten, one of the signed copies filed with the Commission shall be an original "ribbon" copy. Unsigned copies shall be conformed. If the signature of any person is affixed pursuant to a power of attorney or other similar authority, a copy of such power of attorney or other authority shall also be filed with the application or report.

(c) Each copy of an application or report filed with the Commission or with an exchange shall be bound in one or more parts. Copies filed with the Commission shall be bound without stiff covers. The application or report shall be bound on the left side in such a manner as to leave the reading matter legible.

Rule 12b-12. Requirements as to Paper, Printing, and Language.

(a) Applications and reports shall be filed on good quality, unglazed, white paper 8½x13 inches in size, insofar as practicable. However, tables, charts, maps and financial statements may be on larger paper if folded to that size.

(b) The application or report and, insofar as practicable, all papers and documents filed as a part thereof, shall be printed, lithographed, mimeographed, or typewritten. However, the application or report or any portion thereof may be prepared by any similar process which, in the opinion of the Commission, produces copies suitable for a permanent record. Irrespective of the process used, all copies of any such material shall be clear, easily readable and suitable for repeated photocopying. Debits in credit categories and credits in debit categories shall be designated so as to be clearly distinguishable as such on photocopies.

(c) The body of all printed applications and reports shall be in roman type at least as large as ten-point modern type. However, to the extent necessary for convenient presentation, financial statements and other statistical or tabular data and the notes thereto may be in type at least as large as eight-point modern type. All type shall be leaded at least two points.

(d) Applications and reports shall be in the English language. If any exhibit of other paper or document filed with an application or report is in a foreign language, it shall be accompanied by a translation into the English language.

Rule 12b-13. Preparation of Application or Report.

The application or report shall contain the numbers and captions of all items of the appropriate form, but the text of the items may be omitted provided the answers thereto are so prepared as to indicate to the reader the coverage of the items without the necessity of his referring to the text of the items or instructions thereto. However, where any item requires information to be given in tabular form, it shall be given in substantially the tabular form specified in the item. All instructions, whether appearing under the items of the form or elsewhere therein, are to be omitted from the application or report. Unless expressly provided otherwise, if any item is inapplicable or the answer thereto is in the negative, an appropriate statement to that effect shall be made.

Rule 12b-14. Riders—Inserts.

Riders shall not be used. If the application or report is typed on a printed form, and the space provided for the answer to any given item is insufficient, reference shall be made in such space to a full insert page or pages on which the item number and caption and the complete answer are given.

Rule 12b-15. Amendments.

All amendments shall be filed under cover of Form 8 and shall comply with all pertinent requirements applicable to applications and reports. Amendments shall be filed separately for each separate application or report amended. Amendments to an application may be filed either before or after registration becomes effective.

Article 3. General Requirements as to Contents**Rule 12b-20. Additional Information.**

In addition to the information expressly required to be included in an application or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made not misleading.

Rule 12b-21. Information Unknown or Not Available.

Information required need be given only insofar as it is known or reasonably available to the registrant. If any required information is unknown and not reasonably available to the registrant, either because the obtaining thereof would involve unreasonable effort or expense, or because it rests peculiarly within the knowledge of another person not affiliated with the registrant, the information may be omitted, subject to the following conditions:

(a) The registrant shall give such information on the subject as it possesses or can acquire without unreasonable effort or expense, together with the sources thereof.

(b) The registrant shall include a statement either showing that unreasonable effort or expense would be involved or indicating the absence of any affiliation with the person within whose knowledge the information rests and stating the result of a request made to such person for the information.

Rule 12b-22. Disclaimer of Control.

If the existence of control is open to reasonable doubt in any instance, the registrant may disclaim the existence of control and any admission thereof; in such case, however, the registrant shall state the material facts pertinent to the possible existence of control.

Rule 12b-23. Incorporation by Reference.

(a) Matter contained in any part of an application or report, other than exhibits, may be incorporated by reference in answer or partial answer to any item of the application or report. Matter contained in an exhibit may be so incorporated to the extent permitted in Rule 12b-24. An application for registration of additional securities of the registrant (whether of the same or a different class) on the same exchange may incorporate by reference any item contained in any application pursuant to which such prior registration is effective.

(b) Any financial statement filed with the Commission pursuant to any Act administered by the Commission may be incorporated by reference in an application or report filed with the Commission by the same or any other person, if it substantially conforms to the requirements of the form on which the application or report is filed. Any financial statement filed with an exchange pursuant to the Act may be incorporated by reference in any application or report filed with the exchange by the same or any other person, if it substantially conforms to the requirements of the form on which the application or report is filed. If any financial statement filed with the Commission is incorporated by reference in copies of an application or report filed with the Commission pursuant to section 12 or 13 of the Act, copies of the financial statement may be filed with the exchange in lieu of the corresponding financial statement required by the form on which the application or report is filed.

(c) Material incorporated by reference shall be clearly identified in the reference. An express statement that the specified matter is incorporated by reference shall be made at the particular place in the application or report where the information is required. Matter shall not be incorporated by reference in any case where such incorporation would render the statement incomplete, unclear or confusing.

Rule 12b-24. Summaries or Outlines of Documents.

Where an item requires a summary or outline of the provisions of any document, only a brief statement shall be made, in succinct and condensed form, as to the most important provisions of the document. In addition to such statement, the summary or outline may incorporate by reference particular items,

sections, or paragraphs of any exhibit and may be qualified in its entirety by such reference. Matter contained in an exhibit may be incorporated by reference in answer to an item only to the extent permitted by this rule.

Rule 12b-25. Extension of Time for Furnishing Information.

If it is impractical to furnish any required information, document or report at the time it is required to be filed, the registrant may file with the Commission as a separate document an application (a) identifying the information, document or report in question, (b) stating why the filing thereof at the time required is impracticable, and (c) requesting an extension of time for filing the information, document or report to a specified date not more than 60 days after the date it would otherwise have to be filed. The application shall be deemed granted unless the Commission, within 10 days after receipt thereof, shall enter an order denying the application.

Article 4. Exhibits

Rule 12b-30. Additional Exhibits.

The registrant may file such exhibits as it may desire, in addition to those required by the appropriate form. Such exhibits shall be so marked as to indicate clearly the subject matters to which they refer.

Rule 12b-31. Omission of Substantially Identical Documents.

In any case where two or more indentures, contracts, franchises, or other documents required to be filed as exhibits are substantially identical in all material respects except as to the parties thereto, the dates of execution, or other details, the registrant need file a copy of only one of such documents, with a schedule identifying the other documents omitted and setting forth the material details in which such documents differ from the document of which a copy is filed. The Commission may at any time in its discretion require the filing of copies of any document so omitted.

Rule 12b-32. Incorporation of Exhibits by Reference.

(a) Any document or part thereof filed with the Commission pursuant to any Act administered by the Commission may be incorporated by reference as an exhibit to any application or report filed with the Commission by the same or any other person. Any document or part thereof filed with an exchange pursuant to the Act may be incorporated by reference as an exhibit to any application or report filed with the exchange by the same or any other person.

(b) If any modification has occurred in the text of any document incorporated by reference since the filing thereof, the registrant shall file with the reference a statement containing the text of any such modification and the date thereof.

Rule 12b-33. Annual Reports to Other Federal Agencies.

Notwithstanding any rule or other requirement to the contrary, whenever copies of an annual report by a registrant to any other Federal agency are required or permitted to be filed as an exhibit to an application or report filed by such registrant with the Commission or with a securities exchange, only one copy of such annual report need be filed with the Commission and one copy thereof with each such exchange, provided appropriate reference to such copy is made in each copy of the application or report filed with the Commission or with such exchange.

Article 5. Special Provisions

Rule 12b-35. Use of Registration Statement Under Securities Act of 1933.

(a) Any registrant which has effective under the Securities Act of 1933 a registration statement filed on Form S-1 and not subject to any proceeding under section 8 of that Act or to an order entered thereunder may file an application for registration of securities on an exchange consisting of the following:

(1) The registration statement and all amendments thereto filed under the Securities Act of 1933, including financial statements and exhibits, or a composite of such statement as amended. However, any financial statements or exhibits not called for by the appropriate application form may be omitted.

(2) A description of the securities being registered, as required by the appropriate application form, unless they are of the same class as those registered under the statement referred to in subparagraph (1) above.

(3) Any financial statements or exhibits required by the appropriate application form which are not contained in the statement referred to in subparagraph (1) above.

(4) The approximate number of holders of record of each class of stock of the registrant, as of the latest practicable date.

(b) If the registrant has no securities listed and registered on the particular exchange, the application shall also include as exhibits the annual, semi-annual and current reports which would have been required if securities of the registrant had become listed and registered on such exchange on the effective date of the registration statement referred to in subparagraph (a) (1) above. If the registrant has filed reports pursuant to section 13 or 15 (d) of the Act, it may file with the application copies of the reports filed pursuant to that section subsequent to the effective date of such registration statement, in lieu of the reports referred to in the preceding sentence.

(c) If the application for registration is filed more than one year after the effective date of the registration statement referred to in subparagraph (a) (1) above, the information called for by items 3 and 4 of Form 10 shall be included in the application. If the application is filed within one year after the effective date of such registration statement or within one year after the end of the fiscal year covered by the latest annual report furnished pursuant to paragraph (b), the application shall include a brief description of any materially important changes not previously reported, in the business of the registrant and its subsidiaries since the effective date of the registration statement, or since the end of the fiscal year covered by such annual report, as the case may be, including, in the case of an extractive company, any material changes in the reserves of such company. This paragraph shall not apply, however, if the registrant has securities listed and registered on any national securities exchange.

(d) An application for registration filed pursuant to this rule shall be filed under cover of the facing sheet of the appropriate application form and shall be signed in accordance with the requirements of that form. Except as otherwise provided in this rule, all pertinent provisions of these General Rules and Regulations relating to the preparation and filing of applications for registration shall apply to applications filed pursuant to this rule. The following statement and list of contents shall be set forth on the first page of the application immediately following the facing page thereof:

THIS APPLICATION IS FILED PURSUANT TO RULE 12b-35 OF THE GENERAL RULES AND REGULATIONS UNDER THE SECURITIES EXCHANGE ACT OF 1934 AND CONSISTS OF THE FOLLOWING INFORMATION AND DOCUMENTS:

(List the contents of the application for registration, commencing with the registration statement under the Securities Act of 1933, identifying it by file number and effective date.)

(e) In copies of the application filed with the Commission the registrant shall incorporate by reference the registration statement referred to in subparagraph (a) (1) and any reports required by paragraph (b) which are on file with the Commission. If such registration statement or any such annual report incorporates by reference any financial statements or exhibits required by the appropriate form which are on file with the Commission but are not on file with the exchange, copies of the application filed with the exchange shall include copies of such financial statements or exhibits. Rule 12b-36 shall apply to financial statements filed as a part of, or incorporated by reference in, applications for registration filed pursuant to this rule.

(f) Notwithstanding any rule or regulation of the Commission to the contrary, the exhibits required by this form to be physically filed with the exchange may be in photocopy form.

Rule 12b-36. Use of Financial Statements Filed Under Other Acts.

Where copies of certified financial statements filed under other Acts administered by the Commission are filed with an application or report, the accountant's certificate shall be manually signed or manually signed copies of the certificates shall be filed with the financial statements. Where such financial statements are incorporated by reference in an application or report, the written consent of the accountant to such incorporation by reference shall be filed with the application or report. Such consent shall be dated and signed manually.

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REGULATION 13A. REPORTS OF ISSUERS OF LISTED SECURITIES

Article 1. Annual Reports

Rule 13a-1. Requirement of Annual Reports.

Every issuer having securities listed and registered on a national securities exchange shall file an annual report for each fiscal year after the last full fiscal year for which financial statements were filed in its application for registration. Registrants on Form 8-B shall file an annual report for each fiscal year beginning on or after the date as of which the succession occurred. The report shall be filed within 120 days after the close of the fiscal year or within such other period as may be specified in the appropriate form.

Rule 13a-2. Annual Reports of Predecessors.

Every issuer having securities listed and registered pursuant to an application on Form 8-B shall file an annual report pursuant to Rule 13a-1 for each of its predecessors which had securities listed and registered on a national securities exchange, covering the last full fiscal year of the predecessor prior to the registrant's succession, unless such report has been filed by the predecessor. Such annual report shall contain the information that would be required if filed by the predecessor.

Rule 13a-3. Reports in Case of New Registration.

(a) Notwithstanding Rule 13a-1, any registrant which has filed, within the period prescribed for filing an annual report pursuant to that section—

(1) A registration statement under the Securities Act of 1933 which has become effective and is not subject to any proceeding under section 8(d) of that Act or to an order entered thereunder, or

(2) An application for registration of securities on an exchange which has become effective and is not subject to any proceeding under section 19(a) (2) of the Securities Exchange Act of 1934 or to an order thereunder, may file as its annual report pursuant to Rule 13a-1 copies of the registration statement or application in lieu of an annual report on the appropriate annual report form if the statement or application covers the fiscal period that would be covered by a report on the appropriate annual report form and contains all of the information, including financial statements and exhibits, required by the appropriate annual report form.

(b) The report shall be filed under cover of the facing sheet of the appropriate annual report form and shall be signed in accordance with the requirements of that form. The following statement shall appear on the facing sheet of the annual report or on the page immediately following the facing sheet:

"THIS ANNUAL REPORT, FILED PURSUANT TO RULE 13a-3, CONSISTS OF THE INFORMATION AND DOCUMENTS CONTAINED IN THE REGISTRATION STATEMENT (OR APPLICATION FOR REGISTRATION) ON FORM _____, FILED BY THE REGISTRANT ON _____, 19____, AS AMENDED UNDER DATES OF _____."

(c) Any financial statements or exhibits included in the registration statement or application which are not required by the appropriate annual report form may be omitted.

(d) If any registration statement included in the annual report incorporates by reference any financial statements or exhibits required by the appropriate annual report form which are on file with the Commission but are not on file with the exchange, the copies of the annual report filed with the exchange shall include copies of such financial statements or exhibits.

(e) Copies of the report filed with the Commission may incorporate the registration statement or application by reference. If a report consists of an application, copies of the report filed with an exchange with which the application was filed may incorporate the application by reference.

Rule 13a-4. Incorporation of Information Contained in a Prospectus.

Any registrant which has filed with the Commission pursuant to Rule 424 under the Securities Act of 1933 copies of a prospectus meeting the requirements of section 10 of that Act after the effective date of the registration statement may incorporate in its annual report pursuant to Rule 13a-1 any information, including financial statements, contained in the prospectus, provided a copy of the prospectus is filed as an exhibit to the annual report.

Article 2. Other Reports

Rule 13a-10. Interim Reports.

(a) Every issuer which changes its fiscal closing date after the last fiscal year for which financial statements were filed in its application for registration shall file a report covering the resulting interim period not more than 120 days after the close of the interim period or after the date of the determination to change the fiscal closing date, whichever is later.

(b) Every issuer having securities registered pursuant to an application on Form 8-B shall file an interim report for the period, if any, between the close of the fiscal year covered by the last annual report of its predecessor or predecessors and the beginning of the first fiscal year of the registrant subsequent to the succession. The report shall be filed within 120 days after the close of the period. It shall include information regarding the predecessor or predecessors from the close of the most recent fiscal year prior to the succession as if such predecessor or predecessors were the registrant. The financial statements filed with the report shall give effect to the operations of, and transactions by the predecessor or predecessors during the period as if they were the registrant. A statement that effect has been given to such operations and transactions shall be made in a note or otherwise. Separate financial statements for the predecessor or predecessors need not be filed.

(c) A report pursuant to this rule shall be filed on the form appropriate for annual reports of the issuer and shall clearly indicate the period covered. If the report covers an interim period of less than 6 months, the financial statements filed therewith need not be certified but, if they are not certified, the issuer shall file with its next annual report certified financial statements covering the interim period.

(d) Notwithstanding the foregoing, a separate report need not be filed for any period of less than 3 months if the annual report of the issuer or predecessor for the preceding fiscal year or the annual report of the issuer for the succeeding fiscal year covers the interim period as well as the fiscal year. In such case balance sheets need be furnished only as of the close of the entire period but all other financial statements, including balance sheet schedules, shall be filed separately for both periods.

Rule 13a-11. Current Reports on Form 8-K.

(a) Except as provided in paragraph (b), every registrant subject to Rule 13a-1 shall file a current report on Form 8-K within ten days after the close of any month during which any of the events specified in that form occurs, unless substantially the same information as that required by Form 8-K has been previously reported by the registrant.

(b) This section shall not apply to issuers having securities registered on a national securities exchange pursuant to an application on Form 18, 19, 20, or 21, or to investment companies required to file quarterly reports pursuant to Rule 13a-12.

Rule 13a-12. Quarterly Reports of Investment Companies.

Every investment company registered under the Investment Company Act of 1940 which has securities listed and registered on a national securities exchange and for which a quarterly report form is prescribed shall file a quarterly report, on the appropriate form prescribed therefor, for each fiscal quarter for which it is required to file a quarterly report pursuant to section 30(b)(1) of the Investment Company Act of 1940.

Rule 13a-13. Semi-Annual Reports on Form 9-K.

(a) Every issuer of a security registered on a national securities exchange which is required to file annual reports on Form 10-K or Form U5S, or which is required to file a report on one of such forms as Part II of Form 16-K or Form 19-K, shall file a semi-annual report on Form 9-K for the first half of each fiscal year ending after the close of the latest fiscal year for which financial statements of such issuer were filed in an application for registration of securities on a national securities exchange, *provided, however*, that no such report need be filed for any semi-annual period ending prior to June 30, 1955.

(b) Such reports on Form 9-K shall be filed not more than 45 days after the end of the six-month period for which they are filed. However, the report for any period ending prior to the date on which a class of securities of the issuer first becomes effectively registered on a national securities exchange may be filed not more than 45 days after the effective date of such registration.

(c) Notwithstanding paragraph (a) of this rule, semi-annual reports on Form 9-K shall not be required to be filed by the following types of issuers:

- (1) banks and bank holding companies;
- (2) investment companies;
- (3) insurance companies, other than title insurance;
- (4) public utilities and common carriers which file financial reports with the Federal Power Commission, Federal Communications Commission or the Interstate Commerce Commission;
- (5) companies engaged in the seasonal production and seasonal sale of a single-crop agricultural commodity;
- (6) companies in the promotional or development stage to which paragraph (b) or (c) of Rule 5A-01 of Article 5A of Regulation S-X is applicable;
- (7) foreign issuers other than private issuers domiciled in a North American country or Cuba.

(d) Notwithstanding the foregoing paragraphs of this rule, reports pursuant to this rule on Form 9-K shall not be deemed to be "filed" for the purpose of section 18 of the Act or otherwise subject to the liabilities of that section, but shall be subject to all other provisions of the Act.

Rule 13b-1. Carriers and Other Persons Subject to Federal Regulations.

(a) If a person's methods of accounting are prescribed under any law of the United States or any rules and regulations thereunder, the requirements imposed by such law or rules and regulations shall supersede the requirements prescribed by the rules and regulations of the Commission with respect to the same subject matter, insofar as the latter are inconsistent with the former.

(b) Carriers reporting under section 20 of the Interstate Commerce Act, as amended, and carriers required by any other law of the United States to make reports of the same general character as those required under section 20, may file duplicate copies of the reports filed pursuant to such Acts in lieu of any reports, information or documents required by the rules and regulations of the Commission in regard to the same subject matter.

REGULATION 14. SOLICITATION OF PROXIES

Rule 14a-1. Definitions.

Unless the context otherwise requires, all terms used in this regulation have the same meanings as in the Act or elsewhere in the General Rules and Regulations thereunder. In addition, the following definitions apply unless the context otherwise requires:

Associate.—The term "associate" used to indicate a relationship with any person, means (1) any corporation or organization (other than the issuer or a majority-owned subsidiary of the issuer) of which such person is an officer or partner or is, directly or indirectly, the beneficial owner of 10 percent or more of any class of equity securities, (2) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity, and (3) any relative or spouse of such person, or any relative of such spouse, who has the same home as such person or who is a director or officer of the issuer or any of its parents or subsidiaries.

Issuer.—The term "issuer" means the issuer of the securities in respect of which a proxy is solicited.

Last fiscal year.—The term "last fiscal year" of the issuer means the last fiscal year of the issuer ending prior to the date of the meeting for which proxies are to be solicited.

Proxy.—The term "proxy" includes every proxy, consent or authorization within the meaning of section 14 (a) of the Act. The consent or authorization may take the form of failure to object or to dissent.

Proxy statement.—The term "proxy statement" means the statement required by Rule 14a-3(a), whether or not contained in a single document.

Solicitation.—The terms "solicit" and "solicitation" include—

- (1) any request for a proxy whether or not accompanied by or included in a form of proxy;
- (2) any request to execute or not to execute, or to revoke, a proxy; or
- (3) the furnishing of a form of proxy or other communication to security holders under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy.

The terms do not apply, however, to the furnishing of a form of proxy to a security holder upon the unsolicited request of such security holder, the performance by the issuer of acts required by Rule 14a-7, or the performance by any person of ministerial acts on behalf of a person soliciting a proxy.

Rule 14a-2. Solicitations to Which Rules Apply.

The rules contained in this regulation apply to every solicitation of a proxy with respect to securities listed and registered on a national securities exchange, whether or not trading in such securities has been suspended, except the following:

(a) Any solicitation made otherwise than on behalf of the management of the issuer where the total number of persons solicited is not more than 10.

(b) Any solicitation by a person in respect to securities carried in his name or in the name of his nominee (otherwise than as voting trustee) or held in his custody, if such person—

(1) receives no commission or remuneration for such solicitation, directly or indirectly, other than reimbursement of reasonable expenses.

(2) furnishes promptly to the person solicited a copy of all soliciting material with respect to the same subject matter or meeting received from all persons who shall furnish copies thereof for such purpose and who shall, if requested, defray the reasonable expenses to be incurred in forwarding such material, and

(3) in addition, does no more than impartially instruct the person solicited to forward a proxy to the person, if any, to whom the person solicited desires to give a proxy, or impartially request from the person solicited instructions as to the authority to be conferred by the proxy and state that a proxy will be given if no instructions are received by a certain date.

(c) Any solicitation by a person in respect of securities of which he is the beneficial owner.

(d) Any solicitation involved in the offer or sale of a certificate of deposit or other security registered under the Securities Act of 1933.

(e) Any solicitation with respect to a plan of reorganization under Chapter X of the Bankruptcy Act, as amended, if made after the entry of an order approving such plan pursuant to section 174 of said Act and after, or concurrently with, the transmittal of information concerning such plan as required by section 175 of said Act.

(f) Any solicitation which is subject to Rule 62 under the Public Utility Holding Company Act of 1935.

(g) Any solicitation through the medium of a newspaper advertisement which informs security holders of a source from which they may obtain copies of a proxy statement, form of proxy and any other soliciting material and does no more than (1) name the issuer, (2) state the reason for the advertisement, and (3) identify the proposal or proposals to be acted upon by security holders.

Rule 14a-3. Information To Be Furnished Security Holders.

(a) No solicitation subject to this regulation shall be made unless each person solicited its concurrently furnished or has previously been furnished with a written proxy statement containing the information specified in Schedule 14A.

(b) If the solicitation is made on behalf of the management of the issuer and relates to an annual meeting of security holders at which directors are to be elected, each proxy statement furnished pursuant to paragraph (a) shall be accompanied or preceded by an annual report to such security holders containing such financial statements for the last fiscal year as will, in the opinion of the management, adequately reflect the financial position and operations of the issuer. Such annual report, including financial statements, may be in any form deemed suitable by the management. This paragraph shall not apply, however, to solicitations made on behalf of the management before the financial statements are available if solicitation is being made at the time in opposition to the management and if the management's proxy statement includes an undertaking in bold-face type to furnish such annual report to all persons being solicited, at least twenty days before the date of the meeting.

(c) Four copies of each annual report sent to security holders pursuant to this section shall be mailed to the Commission, solely for its information, not later than the date on which such report is first sent or given to security holders or the date on which preliminary copies of solicitation material are filed with the Commission pursuant to Rule 14a-6(a), which ever date is later. The annual report is not deemed to be "soliciting material" or to be "filed" with

the Commission or otherwise subject to this regulation or to the liabilities of section 18 of the Act, except to the extent that the issuer specifically requests that it be treated as a part of the proxy soliciting material or incorporated it in the proxy statement by reference.

Rule 14a-4. Requirements as to Proxy.

(a) The form of proxy (1) shall indicate in bold-face type whether or not the proxy is solicited on behalf of the management, (2) shall provide a specifically designated blank space for dating the proxy and (3) shall identify clearly and impartially each matter or group of related matters intended to be acted upon, whether proposed by the management or by security holders. No reference need be made, however, to proposals as to which discretionary authority is conferred pursuant to paragraph (c).

(b) Means shall be provided in the form of proxy whereby the person solicited is afforded an opportunity to specify by ballot a choice between approval or disapproval of each matter or group of related matters referred to therein as intended to be acted upon, other than elections to office. A proxy may confer discretionary authority with respect to matters as to which a choice is not so specified provided the form of proxy states in bold-face type how it is intended to vote the shares represented by the proxy in each such case.

(c) A proxy may confer discretionary authority with respect to other matters which may come before the meeting, provided the persons on whose behalf the solicitation is made are not aware a reasonable time prior to the time the solicitation is made that any such other matters are to be presented for action at the meeting and provided further that a specific statement to that effect is made in the proxy statement or in the form of proxy. A proxy may also confer discretionary authority with respect to any proposal omitted from the proxy statement and form of proxy pursuant to paragraph (c) of Rule 14a-8.

(d) No proxy shall confer authority (1) to vote for the election of any person to any office for which a bona fide nominee is not named in the proxy statement, or (2) to vote at any annual meeting other than the next annual meeting (or any adjournment thereof) to be held after the date on which the proxy statement and form of proxy are first sent or given to security holders.

(e) The proxy statement or form of proxy shall provide, subject to reasonable specified conditions, that the shares represented by the proxy will be voted and that where the person solicited specifies by means of a ballot provided pursuant to paragraph (b) a choice with respect to any matter to be acted upon, the shares will be voted in accordance with the specifications so made.

Rule 14a-5. Presentation of Information in Proxy Statement.

(a) The information included in the proxy statement shall be clearly presented and the statements made shall be divided into groups according to subject matter and the various groups of statements shall be preceded by appropriate headings. The order of items and sub-items in the schedule need not be followed. Where practicable and appropriate, the information shall be presented in tabular form. All amounts shall be stated in figures. Information required by more than one applicable item need not be repeated. No statement need be made in response to any item or sub-item which is inapplicable.

(b) Any information required to be included in the proxy statement as to terms of securities or other subject matter which from a standpoint of practical necessity must be determined in the future may be stated in terms of present knowledge and intention. To the extent practicable, the authority to be conferred concerning each such matter shall be confined within limits reasonably related to the need for discretionary authority. Subject to the foregoing, information which is not known to the persons on whose behalf the solicitation is to be made and which it is not reasonably within the power of such persons to ascertain or procure may be omitted, if a brief statement of the circumstances rendering such information unavailable is made.

(c) There may be omitted from the proxy statement any information contained in any other proxy soliciting material which has been furnished to each person solicited in connection with the same meeting or subject matter if a clear reference is made to the particular document containing such information.

(d) All printed proxy statements shall be set in roman type at least as large as 10-point modern type except that to the extent necessary for convenient presentation financial statements and other statistical or tabular matter may be set in roman type at least as large as eight-point modern type. All type shall be leaded at least two points.

Rule 14a-6. Material Required To Be Filed.

(a) Three preliminary copies of the proxy statement and form of proxy and any other soliciting material to be furnished to security holders concurrently therewith shall be filed with the Commission at least 10 days prior to the date definitive copies of such material are first sent or given to security holders, or such shorter period prior to that date as the Commission may authorize upon a showing of good cause therefor.

(b) Three preliminary copies of any additional soliciting material, relating to the same meeting or subject matter, furnished to security holders subsequent to the proxy statement shall be filed with the Commission at least 2 days (exclusive of Saturdays, Sundays or holiday) prior to the date copies of such material are first sent or given to security holders, or such shorter period prior to such date as the Commission may authorize upon a showing of good cause therefor.

(c) Four definitive copies of the proxy statement, form of proxy and all other soliciting material, in the form in which such material is furnished to security holders, shall be filed with, or mailed for filing to, the Commission not later than the date such material is first sent or given to any security holders. Three copies of such material shall at the same time be filed with, or mailed for filing to, each national securities exchange upon which any security of the issuer is listed and registered.

(d) If the solicitation is to be made in whole or in part by personal solicitation, three copies of all written instructions or other material which discusses or reviews, or comments upon the merits of, any matter to be acted upon and which is furnished to the individual making the actual solicitation for their use directly or indirectly in connection with the solicitation shall be filed with the Commission by the persons on whose behalf the solicitation is made at least 5 days prior to the date copies of such material are first sent or given to such individuals, or such shorter period prior to that date as the Commission may authorize upon a showing of good cause therefor.

(e) All copies of material filed pursuant to paragraph (a) or (b) shall be clearly marked "Preliminary Copies" and shall be for the information of the Commission only, except that such material may be disclosed to any department or agency of the United States Government and the Commission may make such inquiries or investigation in regard to the material as may be necessary for an adequate review thereof by the Commission. All material filed pursuant to paragraph (a), (b) or (c) shall be accompanied by a statement of the date upon which copies thereof are intended to be, or have been released to security holders. All material filed pursuant to paragraph (d) shall be accompanied by a statement of the date upon which copies thereof are intended to be released to the individuals who will make the actual solicitation.

(f) Copies of replies to inquiries from security holders requesting further information and copies of communications which do no more than request that forms of proxy theretofore solicited be signed and returned need not be filed pursuant to this rule.

(g) Notwithstanding the provisions of paragraphs (a) and (b) of this rule and of paragraph (e) of Rule 14a-11, copies of soliciting material in the form of speeches, press releases and radio or television scripts may, but need not, be filed with the Commission prior to use or publication. Definitive copies, however, shall be filed with or mailed for filing to the Commission as required by paragraph (c) not later than the date such material is used or published. The provisions of paragraphs (a) and (b) of this rule and of paragraph (e) of Rule 14a-11, shall apply, however, to any reprints or reproductions of all or any part of such material.

(h) Where any proxy statement, form of proxy or other material filed pursuant to this rule is amended or revised, two of the copies of such amended or revised material filed pursuant to this rule (or in the case of investment companies registered under the Investment Company Act of 1940, three of such copies) shall be marked to indicate clearly and precisely the changes effected therein. If the amendment or revision alters the text of the material the changes in such text shall be indicated by means of underscoring or in some other appropriate manner.

Note.—Where preliminary copies of material are filed with the Commission pursuant to this rule, the printing of definitive copies for distribution to security holders should be deferred until the comments of the Commission's staff have been received and considered.

Rule 14a-7. Mailing Communications for Security Holders.

If the management of the issuer has made or intends to make any solicitation subject to this regulation, the issuer shall perform such of the following acts as may be duly requested in writing with respect to the same subject matter or meeting by any security holder who is entitled to vote on such matter or to vote at such meeting and who shall defray the reasonable expenses to be incurred by the issuer in the performance of the act or acts requested.

(a) The issuer shall mail or otherwise furnish to such security holder the following information as promptly as practicable after the receipt of such request:

(1) A statement of the approximate number of holders of record of any class of securities, any of the holders of which have been or are to be solicited on behalf of the management, or any group of such holders which the security holder shall designate.

(2) If the management of the issuer has made or intends to make, through bankers, brokers or other persons any solicitation of the beneficial owners of securities of any class, a statement of the approximate number of such beneficial owners, or any group of such owners which the security holder shall designate.

(3) An estimate of the cost of mailing a specified proxy statement, form of proxy or other communication to such holders, including insofar as known or reasonably available, the estimated handling and mailing costs of the bankers, brokers or other persons specified in (2) above.

(b) (1) Copies of any proxy statement, form of proxy or other communication furnished by the security holder shall be mailed by the issuer to such of the holders of record specified in (a) (1) above as the security holder shall designate. The issuer shall also mail to each banker, broker, or other person specified in (a) (2) above a sufficient number of copies of such proxy statement, form of proxy or other communication as will enable the banker, broker, or other person to furnish a copy thereof to each beneficial owner solicited or to be solicited through him.

(2) Any such material which is furnished by the security holder shall be mailed with reasonable promptness by the issuer after receipt of a tender of the material to be mailed, of envelopes or other containers therefor and of postage or payment for postage. The issuer need not, however, mail any such material which relates to any matter to be acted upon at an annual meeting of security holders prior to the earlier of (i) a day corresponding to the first date on which management proxy soliciting material was released to security holders in connection with the last annual meeting of security holders, or (ii) the first day on which solicitation is made on behalf of management. With respect to any such material which relates to any matter to be acted upon by security holders otherwise than at an annual meeting, such material need not be mailed prior to the first day on which solicitation is made on behalf of management.

(3) Neither the management nor the issuer shall be responsible for such proxy statement, form of proxy or other communication.

(c) In lieu of performing the acts specified above, the issuer may, at its option, furnish promptly to such security holder a reasonably current list of the names and addresses of such of the holders of record specified in (a) (1) above as the security holder shall designate, and a list of the names and addresses of such of the bankers, brokers or other persons specified in (a) (2) above as the security holder shall designate together with a statement of the approximate number of beneficial owners solicited or to be solicited through each such banker, broker or other person and a schedule of the handling and mailing costs of each such banker, broker or other persons, if such schedule has been supplied to the management of the issuer. The foregoing information shall be furnished promptly upon the request of the security holder or at daily or other reasonable intervals as it becomes available to the management of the issuer.

Rule 14a-8. Proposals of Security Holders.

(a) If any security holder entitled to vote at a meeting of security holders of the issuer shall submit to the management of the issuer a reasonable time before the solicitation is made a proposal which is accompanied by notice of his intention to present the proposal for action at the meeting, the management shall set forth the proposal in its proxy statement and shall identify the proposal in its form of proxy and provide means by which security holders can make the specification provided for by Rule 14a-4 (b). A proposal so submitted with respect to an annual meeting more than 60 days in advance of a day corresponding to

the first date on which management proxy soliciting material was released to security holders in connection with the last annual meeting of security holders shall prima facie be deemed to have been submitted a reasonable time before the solicitation. This rule shall not apply, however, to elections to office.

(b) If the management opposes the proposal, it shall also, at the request of the security holder, include in its proxy statement the name and address of the security holder and a statement of the security holder in not more than 100 words in support of the proposal. The statement and request of the security holder shall be furnished to the management at the same time that the proposal is furnished. Neither the management nor the issuer shall be responsible for such statement.

(c) Notwithstanding the foregoing, the management may omit a proposal and any statement in support thereof from its proxy statement and form of proxy under any of the following circumstances:

(1) If the proposal as submitted is, under the laws of the issuer's domicile, not a proper subject for action by security holders; or

(2) If it clearly appears that the proposal is submitted by the security holder primarily for the purpose of enforcing a personal claim or redressing a personal grievance against the issuer or its management, or primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes; or

(3) If the management has at the security holder's request included a proposal in its proxy statement and form of proxy relating to either of the last two annual meetings of security holders or any special meeting held subsequent to the earlier of such two annual meetings and such security holder has failed without good cause to present the proposal, in person or by proxy, for action at the meeting; or

(4) If substantially the same proposal has previously been submitted to security holders, in the management's proxy statement and form of proxy relating to any annual or special meeting of security holders held within the preceding five calendar years, it may be omitted from the management's proxy material relating to any meeting of security holders held within the three calendar years after the latest such previous submission, provided that—

(i) If the proposal was submitted at only one meeting during such preceding period, it received less than 3% of the total number of votes cast in regard thereto; or

(ii) if the proposal was submitted at only two meetings during such preceding period it received at the time of its second submission less than 6% of the total number of votes cast in regard thereto; or

(iii) if the proposal was submitted at three or more meetings during such preceding period, it received at the time of its latest submission less than 10% of the total number of votes cast in regard thereto.

(5) If the proposal consists of a recommendation or request that the management take action with respect to a matter relating to the conduct of the ordinary business operations of the issuer.

(d) Whenever the management asserts that a proposal and any statement in support thereof may properly be omitted from its proxy statement and form of proxy, it shall file with the Commission, not later than 20 days prior to the date the preliminary copies of the proxy statement and form of proxy are filed pursuant to Rule 14a-6(a), or such shorter period prior to such date as the Commission may permit, a copy of the proposal and any statement in support thereof as received from the security holder, together with a statement of the reasons why the management deems such omission to be proper in the particular case, and, where such reasons are based on matters of law, a supporting opinion of counsel. The management shall at the same time, if it has not already done so, notify the security holder submitting the proposal of its intention to omit the proposal from its proxy statement and form of proxy and shall forward to him a copy of the statement of the reasons why the management deems the omission of the proposal to be proper and a copy of such supporting opinion of counsel.

Rule 14a-9. False or Misleading Statements.

No solicitation subject to this regulation shall be made by means of any proxy statement, form of proxy, notice of meeting, or other communication, written or oral, containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct

any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading.

Note.—The following are some examples of what, depending upon particular facts and circumstances, may be misleading within the meaning of this rule:

- (a) Predictions as to specific future market values, earnings, or dividends.
- (b) Material which directly or indirectly impugns character, integrity or personal reputation, or directly or indirectly makes charges concerning improper, illegal or immoral conduct or associations, without factual foundation.
- (c) Failure to so identify a proxy statement, form of proxy and other soliciting material as to clearly distinguish it from the soliciting material of any other person or persons soliciting for the same meeting or subject matter.
- (d) Claims made prior to a meeting regarding the results of a solicitation.

Rule 14a-10. Prohibition of Certain Solicitations.

No person making a solicitation which is subject to this regulation shall solicit—

- (a) Any undated or post-dated proxy; or
- (b) Any proxy which provides that it shall be deemed to be dated as of any date subsequent to the date on which it is signed by the security holder.

Rule 14a-11. Special Provisions Applicable to Election Contests.

(a) *Solicitations to which this rule applies.*—This rule applies to any solicitation subject to this regulation by any person or group of persons for the purpose of opposing a solicitation subject to this regulation by any other person or group of persons with respect to the election or removal of directors at any annual or special meeting of security holders.

(b) *Participant or participant in a solicitation.*—For purposes of this rule the terms "participant" and "participant in a solicitation" include the following:

- (1) the issuer;
- (2) any director of the issuer, and any nominee for whose election as a director proxies are solicited;
- (3) any committee or group which solicits proxies, any member of such committee or group, and any person whether or not named as a member who, acting alone or with one or more other persons, directly or indirectly, take the initiative in organizing, directing or financing any such committee or group;
- (4) any person who finances or joins with another to finance the solicitation of proxies, except persons who contribute not more than \$500 and who are not otherwise participants;
- (5) any person who lends money or furnishes credit or enters into any other arrangements, pursuant to any contract or understanding with a participant, for the purpose of financing or otherwise inducing the purchase, sale, holding or voting of securities of the issuer by any participant or other persons, in support of or in opposition to a participant; except that such terms do not include a bank, broker or dealer who, in the ordinary course of business, lends money or executes orders for the purchase or sale of securities and who is not otherwise a participant;
- (6) any other person who solicits proxies: *Provided, however,* That such terms do not include (i) any person or organization retained or employed by a participant to solicit security holders, or any person who merely transmits proxy soliciting material or performs ministerial or clerical duties; (ii) any person employed by a participant in the capacity of attorney, accountant, or advertising, public relations or financial adviser, and whose activities are limited to the performance of his duties in the course of such employment; (iii) any person regularly employed as an officer or employee of the issuer or any of its subsidiaries who is not otherwise a participant; or (iv) any officer or director of, or any person regularly employed by, any other participant, if such officer, director, or employee is not otherwise a participant.

(c) *Filing of information required by Schedule 14B.*—(1) No solicitation subject to this rule shall be made by any person other than the management of an issuer unless at least five business days prior thereto, or such shorter period as the Commission may authorize upon a showing of good cause therefor, there has been filed, with the Commission and with each national securities exchange upon which any security of the issuer is listed and registered, by or on behalf

of each participant in such solicitation, a statement in duplicate containing the information specified by Schedule 14B.

(2) Within five business days after a solicitation subject to this rule is made by the management of an issuer, or such longer period as the Commission may authorize upon a showing of good cause therefor, there shall be filed, with the Commission and with each national securities exchange upon which any security of the issuer is listed and registered, by or on behalf of each participant in such solicitation, other than the issuer, a statement in duplicate containing the information specified by Schedule 14B.

(3) If any solicitation on behalf of management or any other person has been made, or if proxy material is ready for distribution, prior to a solicitation subject to this rule in opposition thereto, a statement in duplicate containing the information specified in Schedule 14B shall be filed by or on behalf of each participant in such prior solicitation, other than the issuer, as soon as reasonably practicable after the commencement of the solicitation in opposition thereto, with the Commission and with each national securities exchange on which any security of the issuer is listed and registered.

(4) If, subsequent to the filing of the statements required by subparagraphs (1), (2), and (3) above, additional persons become participants in a solicitation subject to this rule, there shall be filed, with the Commission and each appropriate exchange, by or on behalf of each such person a statement in duplicate containing the information specified by Schedule 14B, within three business days after such person becomes a participant, or such longer period as the Commission may authorize upon a showing of good cause therefor.

(5) If any material change occurs in the facts reported in any statement filed by or on behalf of any participant, an appropriate amendment to such statement shall be filed promptly with the Commission and each appropriate exchange.

(6) Each statement and amendment thereto filed pursuant to this paragraph (c) shall be part of the official public files of the Commission and for purposes of this regulation shall be deemed a communication subject to the provisions of Rule 14a-9.

(d) *Solicitations prior to furnishing required written proxy statement.*—Notwithstanding the provisions of Rule 14a-3(a), a solicitation subject to this rule may be made prior to furnishing security holders a written proxy statement containing the information specified in Schedule 14A with respect to such solicitation, *Provided That*—

(1) The statements required by paragraph (c) of this rule are filed by or on behalf of each participant in such solicitation.

(2) No form of proxy is furnished to security holders prior to the time the written proxy statement is required by Rule 14a-3(a) is furnished to security holders: *Provided, however,* That this subparagraph (2) shall not apply where a proxy statement then meeting the requirements of Schedule 14A has been furnished to security holders.

(3) At least the information specified in Items 2(a) and 3(a) of the statement required by paragraph (c) to be filed by each participant, or an appropriate summary thereof, is included in each communication sent or given to security holders in connection with the solicitation.

(4) A written proxy statement containing the information specified in Schedule 14A with respect to a solicitation is sent or given security holders at the earliest practicable date.

(e) *Solicitations prior to furnishing required written proxy statement—Filing requirements.*—Three copies of any soliciting material proposed to be sent or given to security holders prior to the furnishing of the written proxy statement required by Rule 14a-3(a) shall be filed with the Commission in preliminary form, at least five business days prior to the date definitive copies of such material with the Commission in preliminary form at least five business days prior to the Commission may authorize upon a showing of good cause therefor.

(f) *Application of this rule to annual report.*—Notwithstanding the provisions of Rule 14a-3(b) and (c), three copies of any portion of the annual report referred to in Rule 14a-3(b) which comments upon or refers to any solicitation subject to this rule, or to any participant in any such solicitation, other than the solicitation by the management, shall be filed with the Commission as proxy material subject to this regulation. Such portion of the annual report shall be filed with the Commission in preliminary form at least five business days prior to the date copies of the report are first sent or given to security holders.

(g) *Application of Rule 14a-6.*—The provisions of paragraphs (c), (d), (e), (f) and (g) of Rule 14a-6 shall apply, to the extent pertinent, to soliciting material subject to paragraphs (e) and (f) of this Rule 14a-11.

(h) *Use of reprints or reproductions.*—In any solicitation subject to this rule, soliciting material which includes, in whole or part, any reprints or reproductions of any previously published material shall:

(1) State the name of the author and publication, the date of prior publication, and identify any person who is quoted without being named in the previously published material.

(2) Except in the case of a public official document or statement, state whether or not the consent of the author and publication has been obtained to the use of the previously published material as proxy soliciting material.

(3) If any participant using the previously published material, or anyone on his behalf, paid, directly or indirectly, for the preparation or prior publication of the previously published material, or has made or proposes to make any payments or give any other consideration in connection with the publication or republication of such material, state the circumstances.

SCHEDULE 14A—INFORMATION REQUIRED IN PROXY STATEMENT

Note.—Where any item calls for information with respect to any matter to be acted upon and such matter involves other matters with respect to which information is called for by other items of this schedule, the information called for by all applicable items shall be given. For example, if action is to be taken with respect to any merger, consolidation or acquisition, specified in Item 14 which involves the election of directors, Items 6 and 7 shall also be answered.

Item 1. Revocability of Proxy.

State whether or not the person giving the proxy has the power to revoke it. If the right of revocation before the proxy is exercised is limited or is subject to compliance with any formal procedure, briefly describe such limitation or procedure.

Item 2. Dissenters' Rights of Appraisal.

Outline briefly the rights of appraisal or similar rights of dissenters with respect to any matter to be acted upon and indicate any statutory procedure required to be followed by dissenting security holders in order to perfect such rights. Where such rights may be exercised only within a limited time after the date of the adoption of a proposal, the filing of a charter amendment or other similar act, state whether the person solicited will be notified of such date.

Item 3. Persons Making the Solicitation.

(a) *Solicitations not subject to Rule 14a-11.*—(1) If the solicitation is made by the management of the issuer, so state. Give the name of any director of the issuer who has informed the management in writing that he intends to oppose any action intended to be taken by the management and indicate the action which he intends to oppose.

(2) If the solicitation is made otherwise than by the management of the issuer, so state and give the names of the persons by whom and on whose behalf it is made.

(3) If the solicitation is to be made otherwise than by the use of the mails, describe the methods to be employed. If the solicitation is to be made by specially engaged employees or paid solicitors, state (i) the material features of any contract or arrangement for such solicitation and identify the parties, and (ii) the cost or anticipated cost thereof.

(4) State the names of the persons by whom the cost of solicitation has been or will be borne, directly or indirectly.

(b) *Solicitations subject to Rule 14a-11.*—(1) State by whom the solicitation is made and describe the methods employed and to be employed to solicit security holders.

(2) If regular employees of the issuer or any other participant in a solicitation have been or are to be employed to solicit security holders, describe the class or classes of employees to be so employed, and the manner and nature of their employment for such purpose.

(3) If specially engaged employees, representatives or other persons have been or are to be employed to solicit security holders, state (i) the material features of any contract or arrangement for such solicitation and identify the parties, (ii) the cost or anticipated cost thereof, and (iii) the approximate number of such employees or employees of any other person (naming such other person) who will solicit security holders.

(4) State the total amount estimated to be spent and the total expenditures to date for, in furtherance of, or in connection with the solicitation of security holders.

(5) State by whom the cost of the solicitation will be borne. If such cost is to be borne initially by any person other than the issuer, state whether reimbursement will be sought from the issuer, and, if so, whether the question of such reimbursement will be submitted to a vote of security holders.

Instruction.—With respect to solicitations subject to Rule 14a-11, costs and expenditures within the meaning of this Item 3 shall include fees for attorneys, accountants, public relations or financial advisers, solicitors, advertising, printing, transportation, litigation and other costs incidental to the solicitation, except that the issuer may exclude the amounts of such costs represented by the amount normally expended for a solicitation for an election of directors in the absence of a contest, and costs represented by salaries and wages of regular employees and officers, provided a statement to that effect is included in the proxy statement.

Item 4. Interest of Certain Persons in Matters To Be Acted Upon.

(a) *Solicitations not subject to Rule 14a-11.*—Describe briefly any substantial interest, direct or indirect, by security holdings or otherwise, of each of the following persons in any matter to be acted upon, other than elections to office:

(1) If the solicitation is made on behalf of management, each person who has been a director or officer of the issuer at any time since the beginning of the last fiscal year.

(2) If the solicitation is made otherwise than on behalf of management, each person on whose behalf the solicitation is made. Any person who would be a participant in a solicitation for purposes of Rule 14a-11 as defined in paragraph (b), (3), (4), (5) (6) thereof shall be deemed a person on whose behalf the solicitation is made for purposes of this paragraph (a).

(3) Each nominee for election as a director of the issuer.

(4) Each associate of the foregoing persons.

Instruction.—Except in the case of a solicitation subject to this regulation made in opposition to another solicitation subject to this regulation, his sub-item (a) shall not apply to any interest arising from the ownership of securities of the issuer where the security holder receives no extra or special benefit not shared on a pro rata basis by all other holders of the same class.

(b) *Solicitations subject to Rule 14a-11.*—(1) Describe briefly any substantial interest, direct or indirect, by security holdings or otherwise, of each participant as defined in Rule 14a-11 (b) (2), (3), (4), (5) and (6), in any matter to be acted upon at the meeting, and include with respect to each participant the information, or a fair and adequate summary thereof, required by Items 2 (a), 2 (d), 3, 4 (b) and 4 (c) of Schedule 14B.

(2) With respect to any person named in answer to Item 6 (b), describe any substantial interest, direct or indirect, by security holdings or otherwise, that he has in any matter to be acted upon at the meeting, and furnish the information called for by Item 4 (b) and (c) of Schedule 14B.

Item 5. Voting Securities and Principal Holders Thereof.

(a) State as to each class of voting securities of the issuer entitled to be voted at the meeting, the number of shares outstanding and the number of votes to which each class is entitled.

(b) Give the date as of which the record of security holders entitled to vote at the meeting will be determined. If the right to vote is not limited to security holders of record on that date, indicate the conditions under which other security holders may be entitled to vote.

(c) If action is to be taken with respect to the election of directors and if the persons solicited have cumulative voting rights, make a statement that they have such rights and state briefly the conditions precedent to the exercise thereof.

(d) If to the knowledge of the persons on whose behalf the solicitation is made, any person owns of record or beneficially more than 10 percent of the outstanding voting securities of the issuer, name such person, state the approximate amount of such securities owned of record but not owned beneficially and the approximate amount owned beneficially by such person and the percentage of outstanding voting securities represented by the amount of securities so owned in each such manner.

Item 6. Nominees and Directors.

(a) If action is to be taken with respect to the election of directors, furnish the following information, in tabular form to the extent practicable, with re-

spect to each person nominated for election as a director and each other person whose term of office as a director will continue after the meeting:

(1) Name each such person, state when his term of office or the term of office for which he is a nominee will expire, and all other positions and offices with the issuer presently held by him, and indicate which persons are nominees for election as directors at that meeting.

(2) State his present principal occupation or employment and give the name and principal business of any corporation or other organization in which such employment is carried on. Furnish similar information as to all of his principal occupations or employments during the last five years, unless he is now a director and was elected to his present term of office by a vote of security holders at a meeting for which proxies were solicited under this regulation.

(3) If he is or has previously been a director of the issuer state the period or periods during which he has served as such.

(4) State, as of the most recent practicable date, the approximate amount of each class of equity securities of the issuer or any of its parents or subsidiaries, other than directors' qualifying shares, beneficially owned directly or indirectly by him. If he is not the beneficial owner of any such securities, make a statement to that effect.

(5) If more than 10% of any class of securities of the issuer or any of its parents or subsidiaries are beneficially owned by him and his associates, state the approximate amount of each class of such securities beneficially owned by such associates, naming each associate whose holdings are substantial.

(b) If any nominee for election as a director is proposed to be elected pursuant to any arrangement or understanding between the nominee and any other person or persons, excepting the directors and officers of the issuer acting solely in that capacity, name such other person or persons and describe briefly such arrangement or understanding.

Item 7. Remuneration and Other Transactions With Management and Others.

Furnish the information called for by this item if action is to be taken with respect to (i) the election of directors, (ii) any bonus, profit sharing or other remuneration plan, contract or arrangement in which any director, nominee for election as a director, or officer of the issuer will participate, (iii) any pension or retirement plan in which any such person will participate, or (iv) the granting or extension to any such person of any options, warrants or rights to purchase any securities, other than warrants or rights issued to security holders, as such, on a pro-rata basis. However, if the solicitation is made on behalf of persons other than the management, the information required need be furnished only as to nominees for election as directors and as to their associates.

(a) Furnish the following information in substantially the tabular form indicated below as to all direct remuneration paid by the issuer and its subsidiaries during the issuer's last fiscal year to the following persons for services in all capacities:

(1) Each director, and each of the three highest paid officers, of the issuer whose direct aggregate remuneration exceeded \$30,000, naming each such person.

(2) All directors and officers of the issuer as a group, without naming them.

(A)	(B)	(C)
Name of individual or identity of group	Capacities in which remuneration was received	Aggregate remuneration

Instructions.—1. This item applies to any person who was a director or officer of the issuer at any time during the period specified. However, information need not be given for any portion of the period during which such person was not a director or officer of the issuer.

2. The information is to be given on an accrual basis if practicable. The tables required by this paragraph and paragraph (b) may be combined if the issuer so desires.

3. Do not include remuneration paid to a partnership in which any director or officer was a partner, but see paragraph (f) below.

(b) Furnish the following information, in substantially the tabular form indicated, as to all pension or retirement benefits proposed to be paid under any existing plan in the event of retirement at normal retirement date, directly

or indirectly, by the issuer or any of its subsidiaries to each director or officer named in answer to paragraph (a) (1) :

(A)	(B)	(C)
Name of individual or identity of group	Amount set aside or accrued during issuer's last fiscal year	Estimated annual benefits upon retirement

Instructions.—1. The term "plan" in this paragraph and in paragraph (c) includes all plans, contracts, authorizations or arrangements, whether or not set forth in any formal document.

2. Column (B) need not be answered with respect to payments computed on an actuarial basis under any plan which provides for fixed benefits in the event of retirement at a specified age or after a specified number of years of service.

3. The information called for by Column (C) may be given in a table showing the annual benefits payable upon retirement to persons in specified salary classifications.

4. In the case of any plan (other than those specified in instruction 2) where the amount set aside each year depends upon the amount of earnings of the issuer or its subsidiaries for such year or a prior year, or where it is otherwise impracticable to state the estimated annual benefits upon retirement, there shall be set forth, in lieu of the information called for by Column (C), the aggregate amount set aside or accrued to date, unless it is impracticable to do so, in which case there shall be stated the method of computing such benefits.

(c) Describe briefly all remuneration payments (other than payments reported under paragraph (a) or (b) of this item) proposed to be made in the future, directly or indirectly, by the issuer or any of its subsidiaries pursuant to any existing plan or arrangement to (i) each director or officer named in answer to paragraph (a) (1), naming each such person, and (ii) all directors and officers of the issuer as a group, without naming them.

Instruction.—Information need not be included as to payments to be made for, or benefits to be received from, group life or accident insurance, group hospitalization or similar group payments or benefits. If it is impracticable to state the amount of remuneration payments proposed to be made, the aggregate amount set aside or accrued to date in respect of such payments shall be stated, together with an explanation of the basis for future payments.

(d) Furnish the following information as to all options to purchase securities, from the issuer or any of its subsidiaries, which were granted to or exercised by the following persons since the beginning of the issuer's last fiscal year: (i) each director or officer named in answer to paragraph (a) (1), naming each such person; and (ii) all directors and officers of the issuer as a group, without naming them:

(1) As to options granted, state (i) the title and amount of securities called for; (ii) the prices, expiration dates and other material provisions; (iii) the consideration received for the granting thereof; and (iv) the market value of the securities called for on the granting date.

(2) As to options exercised, state (i) the title and amount of securities purchased; (ii) the purchase price; and (iii) the market value of the securities purchased on the date of purchase.

Instructions.—1. The term "options" as used in this paragraph (d) includes all options, warrants or rights other than those issued to security holders as such on a pro rata basis.

2. The extension of options shall be deemed the granting of options within the meaning of this paragraph.

3. (i) Where the total market value on the granting dates of the securities called for by all options granted during the period specified does not exceed \$10,000 for any officer or director named in answer to paragraph (a) (1), or \$30,000 for all officers and directors as a group, this item need not be answered with respect to options granted to such person or group. (ii) Where the total market value on the dates of purchase of all securities purchased through the exercise of options during the period specified does not exceed \$10,000 for any such person or \$30,000 for such group, this item need not be answered with respect to options exercised by such person or group.

4. The information for all directors and officers as a group regarding market value of the securities on the granting date of the options and on the purchase date, may be given in the form of price ranges for each calendar quarter during which options were granted or exercised.

(e) State as to each of the following persons who was indebted to the issuer or its subsidiaries at any time since the beginning of the last fiscal year of the issuer, (i) the largest aggregate amount of indebtedness outstanding at any time during such period, (ii) the nature of the indebtedness and of the transaction in which it was incurred, (iii) the amount thereof outstanding as of the latest practicable date, and (iv) the rate of interest paid or charged thereon:

- (1) Each director or officer of the issuer;
- (2) Each nominee for election as a director; and,
- (3) Each associate of any such director, officer or nominee.

Instructions.—1. See instruction 1 to paragraph (a). Include the name of each person whose indebtedness is described and the nature of the relationship by reason of which the information is required to be given.

2. This paragraph does not apply to any person whose aggregate indebtedness did not exceed \$10,000 or 1 percent of the issuer's total assets, whichever is less, at any time during the period specified. Exclude in the determination of the amount of indebtedness all amounts due from the particular person for purchases subject to usual trade terms, for ordinary travel and expense advances and for other transactions in the ordinary course of business.

(f) Describe briefly, and where practicable state the approximate amount of, any material interest, direct or indirect, of any of the following persons in any material transactions since the beginning of the issuer's last fiscal year, or in any material proposed transactions, to which the issuer or any of its subsidiaries was or is to be a party:

- (1) Any director or officer of the issuer;
- (2) Any nominee for election as a director;
- (3) Any security holder named in answer to item 5(d); or
- (4) Any associate of any of the foregoing persons.

Instructions.—1. See instruction 1 to paragraph (a). Include the name of each person whose interest in any transaction is described and the nature of the relationship by reason of which such interest is required to be described. Where it is not practicable to state the approximate amount of the interest, the approximate amount involved in the transaction shall be indicated.

2. As to any transaction involving the purchase or sale of assets by or to the issuer or any subsidiary, otherwise than in the ordinary course of business, state the cost of the assets to the purchaser and the cost thereof to the seller if acquired by the seller within two years prior to the transaction.

3. The instruction to item 4 shall apply to this item.

4. No information need be given under this paragraph as to any remuneration or other transaction reported in response to (a), (b), (c), (d) or (e) of this item.

5. No information need be given under this paragraph as to any transaction or any interest therein where:

(i) The rates or charges involved in the transaction are fixed by law or determined by competitive bids;

(ii) The interest of the specified person in the transaction is solely that of a director of another corporation which is a party to the transaction;

(iii) The transaction involves services as a bank depository of funds, transfer agent, registrar, trustee under a trust indenture, or other similar services;

(iv) The interest of the specified person does not exceed \$30,000; or

(v) The transaction does not involve remuneration for services, directly or indirectly, and (A) the interest of the specified persons arises from the ownership individually and in the aggregate of less than 10% of any class of equity securities of another corporation which is a party to the transaction, (B) the transaction is in the ordinary course of business of the issuer or its subsidiaries, and (C) the amount of such transaction or series of transactions is less than 10% of the total sales or purchases, as the case may be, of the issuer and its subsidiaries.

6. Information shall be furnished under this paragraph with respect to transactions not excluded above which involve remuneration, directly or indirectly, to any of the specified persons for services in any capacity unless the interest of such persons arises solely from the ownership individually and in the aggregate of less than 10% of any class of equity securities of another corporation furnishing the services to the issuer or its subsidiaries.

7. This paragraph (f) does not require the disclosure of any interest in any transaction unless such interest and transaction are material.

Item 8. Selection of Auditors.

If action is to be taken with respect to the selection or approval of auditors, or if it is proposed that particular auditors shall be recommended by any committee to select auditors for whom votes are to be cast, name the auditors and describe briefly any direct financial interest or any material indirect financial interest in the issuer or any of its parents or subsidiaries, or any connection during the past 3 years with the issuer or any of its parents or subsidiaries in the capacity of promoter, underwriter, voting trustee, director, officer or employee.

Item 9. Bonus, Profit Sharing and Other Remuneration Plans.

If action is to be taken with respect to any bonus, profit sharing or other remuneration plan, furnish the following information:

(a) Describe briefly the material features of the plan, identify each class of persons who will participate therein, indicate the approximate number of persons in each such class and state the basis of such participation.

(b) State separately the amounts which would have been distributable under the plan during the last fiscal year of the issuer (1) to directors and officers and (2) to employees if the plan had been in effect.

(c) State the name and position with the issuer of each person specified in item 7(b), who will participate in the plan and the amount which each such person would have received under the plan for the last fiscal year of the issuer if the plan had been in effect.

(d) Furnish such information, in addition to that required by this item and item 7, as may be necessary to describe adequately the provisions already made pursuant to all bonus, profit sharing or other remuneration or incentive plans for (i) each director or officer named in answer to item 7(a) who will participate in the plan to be acted upon; (ii) all directors and officers of the issuer as a group; and (iii) all employees.

(e) If the plan to be acted upon can be amended otherwise than by a vote of stockholders, to increase the cost thereof to the issuer or to alter the allocation of the benefits as between the groups specified in (b), state the nature of the amendments which can be so made.

Instructions.—1. The term "plan" as used in this item means any plan as defined in instruction 1 to item 7 (b).

2. If the plan is set forth in a formal plan, contract or arrangement, three copies thereof shall be filed with the Commission at the time preliminary copies of the proxy statement and form of proxy are filed pursuant to paragraph (a) of Rule 14a-6.

Item 10. Pension and Retirement Plans.

If action is to be taken with respect to any pension or retirement plan, furnish the following information:

(a) Describe briefly the material features of the plan, identify each class of persons who will be entitled to participate therein, indicate the approximate number of persons in each such class and state the basis of such participation.

(b) State (1) the approximate total amount necessary to fund the plan with respect to past services, the period over which such amount is to be paid and the estimated annual payments necessary to pay the total amount over such period, (2) the estimated annual payment to be made with respect to current services and (3) the amount of such annual payments to be made for the benefit of (i) directors and officers and (ii) employees.

(c) State (1) the name and position with the issuer of each person specified in item 7(a) who will be entitled to participate in the plan, (2) the amount which would have been paid to set aside by the issuer and its subsidiaries for the benefit of such person for the last fiscal year of the issuer if the plan had been in effect, and (3) the amount of the annual benefits estimated to be payable to such person in the event of retirement at normal retirement date.

(d) Furnish such information, in addition to that required by this item and item 7, as may be necessary to describe adequately the provisions already made pursuant to all bonus, profit sharing or other remuneration or incentive plans for (i) each director or officer named in answer to item 7(a) who will participate in the plan to be acted upon; (ii) all directors and officers of the issuer as a group; and (iii) all employees.

(e) If the plan to be acted upon can be amended otherwise than by a vote of stockholders to increase the cost thereof to the issuer or alter the allocation of the benefits as between the groups specified in (b) (3), state the nature of the amendments which can be so made.

Instructions.—1. The term "plan" as used in this item means any plan as defined in instruction 1 to item 7 (b).

2. The information called for by paragraph (b) (3) or (c) (2) need not be given as to payments made on an actuarial basis pursuant to any group pension plan which provides for fixed benefits in the event of retirement at a specified age or after a specified number of years of service.

3. If the plan is set forth in a formal plan, contract or other document, three copies thereof shall be filed with the preliminary copies of the proxy statement and form of proxy at the time copies thereof are filed with the Commission pursuant to paragraph (a) of Rule 14a-6.

Item 11. Options, Warrants, or Rights.

If action is to be taken with respect to the granting or extension of any options, warrants or rights to purchase securities of the issuer or any subsidiary, furnish the following information:

(a) State (i) the title and amount of securities called for or to be called for by such options, warrants or rights; (ii) the prices, expiration dates and other material conditions upon which the options, warrants or rights may be exercised; (iii) the consideration received or to be received by the issuer or subsidiary for the granting or extension of the options, warrants or rights; and (iv) the market value of the securities called for or to be called for by the options, warrants or rights, as of the latest practicable date.

(b) State separately the amount of options, warrants or rights received or to be received by the following persons, naming each such person: (i) each director or officer named in answer to item 7 (a); (ii) each nominee for election as a director of the issuer; (iii) each associate of such directors, officers or

nominees; and (iv) each other person who received or is to receive 5% or more of such options, warrants or rights. State also the total amount of such options, warrants or rights received or to be received by all directors and officers of the issuer as a group, without naming them.

(c) Furnish such information, in addition to that required by this item and item 7, as may be necessary to describe adequately the provisions already made pursuant to all bonus, profit sharing or other remuneration or incentive plans for (i) each director or officer named in answer to item 7 (a) who will participate in the plan to be acted upon; (ii) all directors and officers of the issuer as a group; and (iii) all employees.

Instruction.—Paragraphs (b) and (c) do not apply to warrants or rights to be issued to security holder as such on a pro rata basis.

Item 12. Authorization or Issuance of Securities Otherwise Than for Exchange.

If action is to be taken with respect to the authorization or issuance of any securities otherwise than for exchange for outstanding securities of the issuer, furnish the following information:

(a) State the title and amount of securities to be authorized or issued.

(b) Furnish a description of the securities such as would be required to be furnished in an application on the appropriate form for their registration on a national securities exchange. If the securities are additional shares of common stock of a class outstanding, the description may be omitted except for a statement of the preemptive rights, if any.

(c) Describe briefly the transaction in which the securities are to be issued, including a statement as to (1) the nature and approximate amount of consideration received or to be received by the issuer, and (2) the approximate amount devoted to each purpose so far as determinable, for which the net proceeds have been or are to be used.

(d) If the securities are to be issued otherwise than in a general public offering for cash, state the reasons for the proposed authorization or issuance, the general effect thereof upon the rights of existing security holders, and the vote needed for approval.

Item 13. Modification or Exchange of Securities.

If action is to be taken with respect to the modification of any class of securities of the issuer, or the issuance or authorization for issuance of securities of the issuer in exchange for outstanding securities of the issuer, furnish the following information:

(a) If outstanding securities are to be modified, state the title and amount thereof. If securities are to be issued in exchange for outstanding securities, state the title and amount of securities to be so issued, the title and amount of outstanding securities to be exchanged therefor and the basis of the exchange.

(b) Describe any material differences between the outstanding securities and the modified or new securities in respect of any of the matters concerning which information would be required in the description of the securities in an application on the appropriate form for their registration on a national securities exchange.

(c) State the reasons for the proposed modification or exchange, the general effect thereof upon the rights of existing security holders, and the vote needed for approval.

(d) Furnish a brief statement as to arrears in dividends or as to defaults in principal or interest in respect of the outstanding securities which are to be modified or exchanged and such other information as may be appropriate in the particular case to disclose adequately the nature and effect of the proposed action.

(e) Outline briefly any other material features of the proposed modification or exchange. If the plan of proposed action is set forth in a written document, file copies thereof with the Commission in accordance with Rule 14a-6.

Item 14. Mergers, Consolidations, Acquisitions and Similar Matters.

Furnish the following information if action is to be taken with respect to any plan for (i) the merger or consolidation of the issuer into or with any other person or of any other person into or with the issuer, (ii) the acquisition by the issuer or any of its security holders of securities of another issuer, (iii) the acquisition by the issuer of any other going business or of the assets thereof, (iv)

the sale or other transfer of all or any substantial part of the assets of the issuer, or (v) the liquidation or dissolution of the issuer:

(a) Outline briefly the material features of the plan. State the reasons therefor, the general effect thereof upon the rights of existing security holders, and the vote needed for its approval. If the plan is set forth in a written document, file 3 copies thereof with the Commission at the time preliminary copies of the proxy statement and form of proxy are filed pursuant to Rule 14a-6(a).

(b) Furnish the following information as to each person (other than totally-held subsidiaries of the issuer) which is to be merged into the issuer or into or with which the issuer is to be merged or consolidated or the business or assets of which are to be acquired or which is the issuer of securities to be acquired by the issuer in exchange for all or a substantial part of its assets or to be acquired by security holders of the issuer.

(1) Describe briefly the business of such person. Information is to be given regarding pertinent matters such as the nature of the products or services, methods of production, markets, methods of distribution and the sources and supply of raw materials.

(2) State the location and describe the general character of the plants and other important physical properties of such person. The description is to be given from an economic and business standpoint, as distinguished from a legal standpoint.

(3) Furnish a brief statement as to dividends in arrears or defaults in principal or interest in respect of any securities of the issuer or of such person, and as to the effect of the plan thereon and such other information as may be appropriate in the particular case to disclose adequately the nature and effect of the proposed action.

(c) As to each class of securities of the issuer, or of any person specified in paragraph (b), which is admitted to dealing on a national securities exchange or with respect to which a market otherwise exists, and which will be materially affected by the plan, state the high and low sale prices (or, in the absence of trading in a particular period, the range of the bid and asked prices) for each quarterly period within two years. This information may be omitted if the plan involves merely the liquidation or dissolution of the issuer.

Item 15. Financial Statements.

(a) If action is to be taken with respect to any matter specified in item 12, 13, or 14 above, furnish certified financial statements of the issuer and its subsidiaries such as would currently be required in an original application for the registration of securities of the issuer under the Act. All schedules other than the schedules of supplementary profit and loss information may be omitted.

Instruction.—Such statements shall be prepared and certified in accordance with Regulation S-X.

(b) If action is to be taken with respect to any matter specified in item 14(b), furnish financial statements such as would currently be required in an original application by any person specified therein for registration of securities under the Act. Such statements need not be certified and all schedules other than the schedules of supplementary profit and loss information may be omitted. However, such statements may be omitted for (i) a totally-held subsidiary of the issuer which is included in the consolidated statement of the issuer and its subsidiaries, or (ii) a person which is to succeed to the issuer or to the issuer and one or more of its totally-held subsidiaries under such circumstances that Form 8-B would be appropriate for registration of securities of such person issued in exchange for listed securities of the issuer.

(c) Notwithstanding paragraphs (a) and (b) above, any or all of such financial statements which are not material for the exercise of prudent judgment in regard to the matter to be acted upon may be omitted if the reasons for such omission are stated. Such financial statements are deemed material to the exercise of prudent judgment in the usual case involving the authorization or issuance of any material amount of senior securities, but are not deemed material in cases involving the authorization or issuance of common stock, otherwise than in exchange.

(d) The proxy statement may incorporate by reference any financial statements contained in an annual report sent to security holders pursuant to Rule 14a-3 with respect to the same meeting as that to which the proxy statement relates, provided such financial statements substantially meet the requirements of this item.

Item 16. Acquisition or Disposition of Property.

If action is to be taken with respect to the acquisition or disposition of any property, furnish the following information:

- (a) Describe briefly the general character and location of the property.
- (b) State the nature and amount of consideration to be paid or received by the issuer or any subsidiary. To the extent practicable, outline briefly the facts bearing upon the question of the fairness of the consideration.
- (c) State the name and address of the transferor or transferee, as the case may be, and the nature of any material relationship of such person to the issuer or any affiliate of the issuer.
- (d) Outline briefly any other material features of the contract or transaction.

Item 17. Restatement of Accounts.

If action is to be taken with respect to the restatement of any asset, capital, or surplus account of the issuer, furnish the following information:

- (a) State the nature of the restatement and the date as of which it is to be effective.
- (b) Outline briefly the reasons for the restatement and for the selection of the particular effective date.
- (c) State the name and amount of each account (including any reserve accounts) affected by the restatement and the effect of the restatement thereon.
- (d) To the extent practicable, state whether and the extent, if any, to which the restatement will, as of the rate thereof, alter the amount available for distribution to the holders of equity securities.

Item 18. Action With Respect to Reports.

If action is to be taken with respect to any report of the issuer or its directors, officers or committees or any minutes of meeting of its stockholders, furnish the following information:

- (a) State whether or not such action is to constitute approval or disapproval of any of the matters referred to in such reports or minutes.
- (b) Identify each of such matters which it is intended will be approved or disapproved, and furnish the information required by the appropriate item or items of this schedule with respect to each such matter.

Item 19. Matters Not Required To Be Submitted.

If action is to be taken with respect to any matter which is not required to be submitted to a vote of security holders, state the nature of such matter, the reasons for submitting it to a vote of security holders and what action is intended to be taken by the management in the event of a negative vote on the matter by the security holders.

Item 20. Amendment of Charter, By-Laws or Other Documents.

If action is to be taken with respect to any amendment of the issuer's charter, by-laws or other documents as to which information is not required above, state briefly the reasons for and general effect of such amendment and the vote needed for its approval.

Item 21. Other Proposed Action.

If action is to be taken with respect to any matter not specifically referred to above describe briefly the substance of each such matter in substantially the same degree of detail as is required by items 5 to 20, inclusive, above.

SCHEDULE 14B—INFORMATION TO BE INCLUDED IN STATEMENTS FILED BY OR ON BEHALF OF A PARTICIPANT (OTHER THAN THE ISSUER) IN A PROXY SOLICITATION PURSUANT TO RULE 14a-11 (c)

Answer every item. If an item is inapplicable or the answer is in the negative, so state. The information called for by items 2 (a) and 3 (a) or a fair summary thereof is required to be included in all preliminary soliciting material by Rule 14a-11 (d).

Item 1. Issuer.

State the name and address of the issuer.

Item 2. Identity and Background.

- (a) State the following:
 - (1) Your name and business address.

(2) Your present principal occupation or employment and the name, principal business and address of any corporation or other organization in which such employment is carried on.

(b) State the following:

(1) Your residence address.

(2) Information as to all material occupations, positions, offices or employments during the last ten years, giving starting and ending dates of each and the name, principal business and address of any business corporation or other business organization in which each such occupation, position, office or employment was carried on.

(c) State whether or not you are or have been a participant in any other proxy contest involving this or other issuers within the past ten years. If so, identify the principals, the subject matter and your relationship to the parties and the outcome.

(d) State whether or not, during the past ten years, you have been convicted in a criminal proceeding (excluding traffic violations or similar misdemeanors) and, if so, give dates, nature of conviction, name and location of court, and penalty imposed or other disposition of the case. A negative answer to this sub-item need not be included in the proxy statement or other proxy soliciting material.

Item 3. Interests in Securities of the Issuer.

(a) State the amount of each class of securities of the issuer which you own beneficially, directly or indirectly.

(b) State the amount of each class of securities of the issuer which you own of record but not beneficially.

(c) State with respect to the securities specified in (a) and (b) the amounts acquired within the past two years, the dates of acquisition and the amounts acquired on each date.

(d) If any part of the purchase price or market value of any of the shares specified in paragraph (c) is represented by funds borrowed or otherwise obtained for the purpose of acquiring or holding such securities, so state and indicate the amount of the indebtedness as of the latest practicable date. If such funds were borrowed or obtained otherwise than pursuant to a margin account or bank loan in the regular course of business of a bank, broker or dealer, briefly describe the transaction, and state the names of the parties.

(e) State whether or not you are a party to any contracts, arrangements or understandings with any person with respect to any securities of the issuer, including but not limited to joint ventures, loan or option arrangements, puts or calls, guarantees against loss or guarantees of profits, division of losses or profits, or the giving or withholding of proxies. If so, name the persons with whom such contracts, arrangements, or understandings exist and give the details thereof.

(f) State the amount of securities of the issuer owned beneficially, directly or indirectly, by each of your associates and the name and address of each such associate.

(g) State the amount of each class of securities of any parent or subsidiary of the issuer which you own beneficially, directly or indirectly.

Item 4. Further Matters.

(a) Describe the time and circumstances under which you became a participant in the solicitation and state the nature and extent of your activities or proposed activities as a participant.

(b) Furnish for yourself and your associates the information required by item 7 (f) of Schedule 14A.

(c) State whether or not you or any of your associates have any arrangement or understanding with any person—

(1) with respect to any future employment by the issuer or its affiliates; or

(2) with respect to any future transactions to which the issuer or any of its affiliates will or may be a party.

If so, describe such arrangement or understanding and state the names of the parties thereto.

Item 5. Signature.

The statement shall be dated and signed in the following manner :

I certify that the statements made in this statement are true, complete, and correct, to the best of my knowledge and belief.

(Date)

(Signature of participant or authorized representative)

Instruction.—If the statement is signed on behalf of a participant by the latter's authorized representative, evidence of the representative's authority to sign on behalf of such participant shall be filed with the statement.

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INSPECTION AND PUBLICATION OF INFORMATION FILED UNDER THE ACT

Rule 24b-1. Documents To Be Kept Public by Exchanges.

Upon action of the Commission granting an exchange's process application for registration or exemption, the exchange shall make available to public inspection at its offices during reasonable office hours a copy of the statement and exhibits filed with the Commission (including any amendments thereto) except those portions thereof to the disclosure of which the exchange shall have filed objection pursuant to Rule 24b-2 which objection shall not have been overruled by the Commission pursuant to section 24 (b).

Rule 24b-2. Nondisclosure of Information Filed With the Commission and With an Exchange.

Any person filing any application, report, or document under the Act may make written objection to the public disclosure of any information contained therein in accordance with the procedure set forth below :

(a) The person shall omit from the application, report, or document, when it is filed, the portion thereof which it desires to keep undisclosed (hereinafter called the confidential portion). In lieu thereof, it shall indicate at the appropriate place in the application, report, or document that the confidential portion has been so omitted and filed separately with the Commission.

(b) The person shall file with the copies of the application, report, or document filed with the Commission—

(1) As many copies of the confidential portion, each clearly marked "CONFIDENTIAL TREATMENT," as there are copies of the application, report, or document filed with the Commission and with each exchange. Each copy shall contain the complete text of the item and, notwithstanding that the confidential portion does not constitute the whole of the answer, the entire answer thereto; except that in case the confidential portion is part of a financial statement or schedule, only the particular financial statement or schedule need be included. All copies of the confidential portion shall be in the same form as the remainder of the application, report, or document.

(2) An application making objection to the disclosure of the confidential portion. Such application shall be on a sheet or sheets separate from the confidential portion, and shall contain: (i) An identification of the portion of the application, report, or document which has been omitted; (ii) a statement of the grounds of objection; (iii) either a consent that the Commission shall determine the question of public disclosure upon the basis of the application and without a hearing, or a request for a hearing on the question of public disclosure, if that is desired; (iv) the name of each exchange with which the application, report, or document is filed.

The copies of the confidential portion and the application filed in accordance with this paragraph (b) shall be enclosed in a separate envelope marked "CONFIDENTIAL TREATMENT" and addressed to The Chairman, Securities and Exchange Commission, Washington 25, D.C.

(c) Pending the determination by the Commission as to the objection filed in accordance with paragraph (b), the confidential portion will be kept undisclosed.

(d) If the Commission determines that the objection shall be sustained, a notation to that effect will be made at the appropriate place in the application, report, or document.

(e) Prior to any determination overruling the objection, if a hearing shall have been requested in accordance with paragraph (b), at least 10 days' notice of the time and place of such hearing will be given by registered mail to the person or his agent for service. Failure of any person making an application pursuant to paragraph (b) to request a hearing, to appear at such hearing, or to offer evidence at the hearing in support of his application, shall be deemed a consent by such person to the submission of his objection for determination by the Commission. In any case in which a hearing has been held, the Commission need consider only such grounds of objection as shall have been supported by evidence adduced at the hearing and the failure at the hearing to adduce evidence in support of any ground of objection may be deemed by the Commission a waiver thereof.

(f) If after such hearing the Commission determines that the objection shall be sustained, a notation to that effect will be made at the appropriate place in the application, report, or document.

(g) If such hearing either (i) shall not have been requested, or (ii) if requested, shall have been held, and the Commission shall have determined that disclosure of the confidential portion is in the public interest, a finding and determination to that effect will be entered and notice of the finding and determination will be sent by registered mail to the person or his agent for service.

(h) If such finding and determination are made with respect to the confidential portion of an application, report, or document filed pursuant to section 12 or 13 of the Act, the registration of the securities with respect to which the application, report, or document was filed may be withdrawn at any time within fifteen days of the dispatch of notice by registered mail of such finding and determination. Such withdrawal shall be effected as follows:

(1) The issuer shall file with the Commission a written notification of withdrawal.

(2) Upon receipt of such notification, the Commission will send confirmed telegraphic notice thereof to each exchange on which the securities are registered.

(3) The registration shall continue in effect until, and shall terminate on, the close of business of the tenth day after the dispatch of such telegraphic notice to the exchange by the Commission.

(4) All applications, reports, or documents filed in connection with the registration shall be retained by the Commission and the exchange on which filed, and shall be plainly marked: "Registration withdrawn as of _____ (date of termination of registration)" except that all copies of the confidential portion will be returned to the issuer.

(i) The confidential portion shall be made available to the public at the time and according to the conditions specified below:

(1) Upon the lapse of fifteen days after the dispatch of notice by registered mail of the finding and determination of the Commission described in paragraph (g), if prior to the lapse of such fifteen days the person shall not have filed a written statement that he intends in good faith to seek judicial review of the finding and determination;

(2) Upon the lapse of sixty days after the dispatch of notice by registered mail of the finding and determination of the Commission, if the statement described in subparagraph (1) immediately above shall have been filed and if a petition for review shall not have been filed within such sixty days; or

(3) If such petition for review shall have been filed within such sixty days, upon final disposition, adverse to the person, of the judicial proceedings.

(j) If the confidential portion is made available to the public, one copy thereof shall be attached to each copy of the application, report, or document filed with the Commission and with each exchange.

Rule 24b-3. Information Filed by Issuers and Others Under Sections 12, 13, 14, and 16.

(a) Except as otherwise provided in this rule and in Rule 17a-6, each exchange shall keep available to the public, under reasonable regulations as to the manner of inspection, during reasonable office hours, all information regarding a security registered on such exchange which is filed with it pursuant to sections 12, 13, 14, or 16, or any rules or regulations thereunder. This requirement shall not apply to any information to the disclosure of which objection has been filed pursuant to Rule 24b-2, which objection shall not have been overruled by the Commission pursuant to section 24(b). The making of such information avail-

able pursuant to this rule shall not be deemed a representation by any exchange as to the accuracy, completeness, or genuineness thereof.

(b) In the case of an application for registration of a security pursuant to section 12 an exchange may delay making available the information contained therein until it has certified to the Commission its approval of such security for listing and registration.

* * * * *

[From Investment Company Act of 1940]

Transactions of Certain Affiliated Persons and Underwriters

SEC. 17. (a) It shall be unlawful for any affiliated person or promoter of or principal underwriter for a registered investment company (other than a company of the character described in section 12 (d) (3) (A) and (B)), or any affiliated person or such a person, promoter, or principal underwriter, acting as principal—

(1) knowingly to sell any security or other property to such registered company or to any company controlled by such registered company, unless such sale involves solely (A) securities of which the buyer is the issuer, (B) securities of which the seller is the issuer and which are part of a general offering to the holders of a class of its securities, or (C) securities deposited with the trustee of a unit investment trust or periodic payment plan by the depositor thereof;

(2) knowingly to purchase from such registered company, or from any company controlled by such registered company, any security or other property (except securities of which the seller is the issuer); or

(3) to borrow money or other property from such registered company or from any company controlled by such registered company (unless the borrower is controlled by the lender) except as permitted in section 21 (b).

(b) Notwithstanding subsection (a), any person may file with the Commission an application for an order exempting a proposed transaction of the applicant from one or more provisions of that subsection. The Commission shall grant such application and issue such order of exemption if evidence establishes that—

(1) the terms of the proposed transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned;

(2) the proposed transaction is consistent with the policy of each registered investment company concerned, as recited in its registration statement and reports filed under this title; and

(3) the proposed transaction is consistent with the general purposes of this title.

(c) Notwithstanding subsection (a), a person may, in the ordinary course of business, sell to or purchase from any company merchandise or may enter into a lessor-lessee relationship with any person and furnish the services incident thereto.

(d) It shall be unlawful for any affiliated person of or principal underwriter for a registered investment company (other than a company of the character described in section 12(d) (3) (A) and (B)), or any affiliated person of such a person or principal underwriter, acting as principal to effect any transaction in which such registered company, or a company controlled by such registered company, is a joint or a joint and several participant with such person, principal underwriter, or affiliated person, in contravention of such rules and regulations as the Commission may prescribe for the purpose of limiting or preventing participation by such registered or controlled company on a basis different from or less advantageous than that of such other participant. Nothing contained in this subsection shall be deemed to preclude any affiliated person from acting as manager of any underwriting syndicate or other group in which such registered or controlled company is a participant and receiving compensation therefor.

(e) It shall be unlawful for any affiliated person of a registered investment company, or any affiliated person of such person—

(1) acting as agent, to accept from any source any compensation (other than a regular salary or wages from such registered company) for the purchase or sale of any property to or for such registered company or any con-

trolled company thereof, except in the course of such person's business as an underwriter or broker; or

(2) acting as broker, in connection with the sale of securities to or by such registered company or any controlled company thereof, to receive from any source a commission, fee, or other remuneration for effecting such transaction which exceeds (A) the usual and customary broker's commission if the sale is effected on a securities exchange, or (B) 2 per centum of the sales price if the sale is effected in connection with a secondary distribution of such securities, or (C) 1 per centum of the purchase or sale price of such securities if the sale is otherwise effected unless the Commission shall, by rules and regulations or order in the public interest and consistent with the protection of investors, permit a larger commission.

(f) Every registered management company shall place and maintain its securities and similar investments in the custody of (1) a bank having the qualifications prescribed in paragraph (1) of section 26(a) for the trustees of unit investment trusts; or (2) a company which is a member of a national securities exchange as defined in the Securities Exchange Act of 1934, subject to such rules and regulations as the Commission may from time to time prescribe for the protection of investors; or (3) such registered company, but only in accordance with such rules and regulations or orders as the Commission may from time to time prescribe for the protection of investors. Rules, regulations, and orders of the Commission under this subsection, among other things, may make appropriate provision with respect to such matters as the earmarking, segregation, and hypothecation of such securities and investments, and may provide for or require periodic or other inspections by any or all of the following: Independent public accountants, employees and agents of the Commission, and such other persons as the Commission may designate. No such member which trades in securities for its own account may act as custodian except in accordance with rules and regulations prescribed by the Commission for the protection of investors.

(g) The Commission is authorized to require by rules and regulations or orders for the protection of investors that any officer and employee of a registered management investment company who may singly, or jointly with others, have access to securities or funds of any registered company, either directly or through authority to draw upon such funds or to direct generally the disposition of such securities, be bonded by a reputable fidelity insurance company against larceny and embezzlement in such reasonable minimum amounts as the Commission may prescribe.

(h) After one year from the effective date of this title, neither the charter, certificate of incorporation, articles of association, indenture of trust, nor the by-laws of any registered investment company, nor any other instrument pursuant to which such a company is organized or administered, shall contain any provision which protects or purports to protect any director or officer of such company against any liability to the company or to its security holders to which he would otherwise be subject by reason of willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of his office.

In the event that any such instrument does not at the effective date of this Act comply with the requirements of this subsection (h) and is not amended to comply therewith prior to the expiration of said one year, such company may nevertheless continue to be a registered investment company and shall not be deemed to violate this subsection if prior to said expiration date each such director or officer shall have filed with the Commission a waiver in writing of any protective provision of the instrument to the extent that it does not comply with this subsection, and each such person subsequently elected or appointed shall before assuming office file a similar waiver.

(i) After one year from the effective date of this title no contract or agreement under which any person undertakes to act as investment adviser of, or principal underwriter for, a registered investment company shall contain any provision which protects or purports to protect such person against any liability to such company or its security holders to which he would otherwise be subject by reason of willful misfeasance, bad faith, or gross negligence, in the performance of his duties, or by reason of his reckless disregard of his obligations and duties under such contract or agreement.

In the event that any such contract or agreement does not at the effective date of this Act comply with the requirements of this subsection (i) and is not amended to comply therewith prior to the expiration of said one year, this subsection shall not be deemed to have been violated if prior to said expiration date each such investment adviser or principal underwriter shall have filed

with the Commission a waiver in writing of any protective provision of the contract or agreement to the extent that it does not comply with this subsection.

* * * * *

Proxies; Voting Trusts; Circular Ownership

SEC. 20. (a) It shall be unlawful for any person, by use of the mails or any means or instrumentality of interstate commerce or otherwise, to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security of which a registered investment company is the issuer in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) It shall be unlawful for any registered investment company or affiliated person thereof, any issuer of a voting-trust certificate relating to any security of a registered investment company, or any underwriter of such a certificate, by use of the mails or any means or instrumentality of interstate commerce, or otherwise, to offer for sale, sell, or deliver after sale, in connection with a public offering, any such voting-trust certificate. The prohibitions of this subsection shall not apply to a class of voting-trust certificates, if any certificate of such class was made the subject of a public offering by the issuer or by or through an underwriter prior to March 15, 1940.

(c) No registered investment company shall purchase any voting security if, to the knowledge of such registered company, cross-ownership or circular ownership exists, or after such acquisition will exist, between such registered company and the issuer of such security. Cross-ownership shall be deemed to exist between two companies when each of such companies beneficially owns more than 3 per centum of the outstanding voting securities of the other company. Circular ownership shall be deemed to exist between two companies if such companies are included within a group of three or more companies, each of which—

(1) beneficially owns more than 3 per centum of the outstanding voting securities of one or more other companies of the group; and

(2) has more than 3 per centum of its own outstanding voting securities beneficially owned by another company, or by each of two or more other companies, of the group.

(d) If on the effective date of this title cross-ownership or circular ownership exists between a registered investment company and any other company or companies, it shall be the duty of such registered company, within five years after such effective date, to eliminate such cross-ownership or circular ownership. If at any time after the effective date of this title cross-ownership or circular ownership between a registered investment company and any other company or companies comes into existence upon the purchase by a registered investment company of the securities of another company, it shall be the duty of such registered company, within one year after it first knows of the existence of such cross-ownership or circular ownership, to eliminate the same.

Loans

SEC. 21. It shall be unlawful for any registered management company to lend money or property to any person, directly or indirectly, if—

(a) the investment policies of such registered company, as recited in its registration statement and reports filed under this title, do not permit such a loan; or

(b) such person controls or is under common control with such registered company; except that the provisions of this paragraph shall not apply to the extension or renewal of any such loan made prior to March 15, 1940, or to any loan from a registered company to a company which owns all of the outstanding securities of such registered company, except directors' qualifying shares.

* * * * *

Registration of Securities Under Securities Act of 1933

SEC. 24. (a) In registering under the Securities Act of 1933 any security of which it is the issuer, a registered investment company, in lieu of furnishing a registration statement containing the information and documents specified in schedule A of said Act, may file a registration statement containing the following information and documents:

(1) such copies of the registration statement filed by such company under this title, and of such reports filed by such company pursuant to section 30 or such copies of portions of such registration statement and reports, as the Commission shall designate by rules and regulations; and

(2) such additional information and documents (including a prospectus) as the Commission shall prescribe by rules and regulations as necessary or appropriate in the public interest or for the protection of investors.

(b) It shall be unlawful for any of the following companies, or for any underwriter for such a company, in connection with a public offering of any security of which such company is the issuer, to make use of the mails or any means or instrumentalities of interstate commerce, to transmit any advertisement, pamphlet, circular, form letter, or other sales literature addressed to or intended for distribution to prospective investors unless three copies of the full text thereof have been filed with the Commission or are filed with the Commission within ten days thereafter:

- (1) any registered open-end company;
- (2) any registered unit investment trust; or
- (3) any registered face-amount certificate company.

(c) In addition to the powers relative to prospectuses granted the Commission by section 10 of the Securities Act of 1933, the Commission is authorized to require, by rules and regulations or order, that the information contained in any prospectus relating to any periodic payment plan certificate or face-amount certificate registered under the Securities Act of 1933 on or after the effective date of this title be presented in such form and order of items, and such prospectus contain such summaries of any portion of such information, as are necessary or appropriate in the public interest or for the protection of investors.

(d) The exemption provided by paragraph (8) of section 3(a) of the Securities Act of 1933 shall not apply to any security of which an investment company is the issuer. The exemption provided by paragraph (11) of said section 3(a) shall not apply to any security of which a registered investment company is the issuer, except a security sold or disposed of by the issuer or bona fide offered to the public prior to the effective date of this title, and with respect to a security so sold, disposed of, or offered, shall not apply to any new offering thereof on or after the effective date of this title. The exemption provided by the third clause of section 4(1) of the Securities Act of 1933, as amended, shall not apply to any transaction in a security issued by a face-amount certificate company or in a redeemable security issued by an open-end management company or unit investment trust, if any other security of the same class is currently being offered or sold by the issuer or by or through an underwriter in a distribution which is not exempted from section 5 of said Act, except to such extent and subject to such terms and conditions as the Commission, having due regard for the public interest and the protection of investors, may prescribe by rules or regulations with respect to any class of persons, securities, or transactions.¹

(e) (1) A registration statement under the Securities Act of 1933 relating to a security issued by a face-amount certificate company or a redeemable security issued by an open-end management company or unit investment trust may be amended after its effective date so as to increase the securities specified therein as proposed to be offered. At the time of filing such amendment there shall be paid to the Commission a fee, calculated in the manner specified in section 6(b) of said Act, with respect to the additional securities therein proposed to be offered.

(2) The filing of such an amendment to a registration statement under the Securities Act of 1933 shall not be deemed to have taken place unless it is accompanied by a United States postal money order or a certified bank check or cash for the amount of the fee required under paragraph (1) of this subsection.

(3) For the purposes of section 11 of the Securities Act of 1933, as amended, the effective date of the latest amendment filed pursuant to this subsection or otherwise shall be deemed the effective date of the registration statement with respect to securities sold after such amendment shall have become effective. For the purposes of section 13 of the Securities Act of 1933, as amended, no such security shall be deemed to have been bona fide offered to the public prior to the effective date of the latest amendment filed pursuant to this subsection. Except to the extent the Commission otherwise provides by rules or regulations as appro-

¹ The last sentence of this subsection was added by Public No. 577, 83d Congress (68 Stat. 689).

ropriate in the public interest or for the protection of investors, no prospectus relating to a security issued by a face-amount certificate company or a redeemable security issued by an open-end management company or unit investment trust which varies for the purposes of subsection (a) (3) of section 10 of the Securities Act of 1933 from the latest prospectus filed as a part of the registration statement shall be deemed to meet the requirements of said section 10 unless filed as part of an amendment to the registration statement under said Act and such amendment has become effective.²

* * * * *

Periodic and Other Reports; Reports of Affiliated Persons

SEC. 30. (a) Every registered investment company shall file annually with the Commission such information, documents, and reports as investment companies having securities registered on a national securities exchange are required to file annually pursuant to section 13 (a) of the Securities Exchange Act of 1934 and the rules and regulations issued thereunder.

(b) Every registered investment company shall file with the commission—

(1) such information and documents (other than financial statements) as the Commission may require, on a semi-annual or quarterly basis, to keep reasonably current the information and documents contained in the registration statement of such company filed under this title; and

(2) copies of every periodic or interim report or similar communication containing financial statements and transmitted to any class of such company's security holders, such copies to be filed not later than ten days after such transmission.

Any information or documents contained in a report or other communication to security holders filed pursuant to paragraph (2) may be incorporated by reference in any report subsequently or concurrently filed pursuant to paragraph (1).

(c) The Commission shall issue rules and regulations permitting the filing with the Commission, and with any national securities exchange concerned, of copies of periodic reports, or of extracts therefrom, filed by any registered investment company pursuant to subsections (a) and (b), in lieu of any reports and documents required of such company under section 13 or 15 (d) of the Securities Exchange Act of 1934.

(d) Every registered investment company shall transmit to its stockholders, at least semi-annually, reports containing such of the following information and financial statements or their equivalent, as of a reasonably current date, as the Commission may prescribe by rules and regulations for the protection of investors, which reports shall not be misleading in any material respect in the light of the reports required to be filed pursuant to subsections (a) and (b):

(1) a balance sheet accompanied by a statement of the aggregate value of investments on the date of such balance sheet;

(2) a list showing the amounts and values of securities owned on the date of such balance sheet;

(3) a statement of income, for the period covered by the report, which shall be itemized at least with respect to each category of income and expense representing more than 5 per centum of total income or expense;

(4) a statement of surplus, which shall be itemized at least with respect to each charge or credit to the surplus account which represents more than 5 per centum of the total charges or credits during the period covered by the report;

(5) a statement of the aggregate remuneration paid by the company during the period covered by the report (A) to all directors and to all members of any advisory board for regular compensation; (B) to each director and to each member of an advisory board for special compensation; (C) to all officers; and (D) to each person of whom any officer or director of the company is an affiliated person; and

(6) a statement of the aggregate dollar amounts of purchases and sales of investment securities, other than Government securities, made during the period covered by the report:

Provided, That if in the judgment of the Commission any item required under this subsection is inapplicable or inappropriate to any specified type or types

² Subsection (e) was added by Public No. 577, 83d Congress (68 Stat. 689).

of investment company, the Commission may by rules and regulations permit in lieu thereof the inclusion of such item of a comparable character as it may deem applicable or appropriate to such type or types of investment company.

(e) Financial statements contained in annual reports required pursuant to subsections (a) and (d), if required by the rules and regulations of the Commission, shall be accompanied by a certificate of independent public accountants. The certificate of such independent public accountants shall be based upon an audit not less in scope or procedures followed than that which independent public accountants would ordinarily make for the purpose of presenting comprehensive and dependable financial statements, and shall contain such information as the Commission may prescribe, by rules and regulations in the public interest or for the protection of investors, as to the nature and scope of the audit and the findings and opinion of the accountants. Each such report shall state that such independent public accountants have verified securities owned, either by actual examination, or by receipt of a certificate from the custodian, as the Commission may prescribe by rules and regulations.

(f) Every person who is directly or indirectly the beneficial owner of more than 10 per centum of any class of outstanding securities (other than short-term paper) of which a registered closed-end company is the issuer or who is an officer, director, member of an advisory board, investment adviser, or affiliated person of an investment adviser of such a company shall in respect of his transactions in any securities of such company (other than short-term paper) be subject to the same duties and liabilities as those imposed by section 16 of the Securities Exchange Act of 1934 upon certain beneficial owners, directors, and officers in respect of their transactions in certain equity securities.

* * * * *

Rules Under Section 17

Rule 17a-1. Exemption of Certain Underwriting Transactions Exempted by Rule 10f-1.

Any transaction exempted pursuant to Rule 10f-1 shall be exempt from the provisions of Section 17(a) (1) of the Act.

Rule 17a-2. Exemption of Certain Purchase, Sale, or Borrowing Transactions.

Purchase, sale or borrowing transactions occurring in the usual course of business between affiliated persons of registered investment companies shall be exempt from Section 17(a) of the Act provided (1) the transactions involve notes, drafts, time payment contracts, bills of exchange, acceptances or other property of a commercial character rather than of an investment character; (2) the buyer or lender is a bank; and (3) the seller or borrower is a bank or is engaged principally in the business of installment financing.

Rule 17a-3. Exemption of Transactions With Fully-Owned Subsidiaries.

(a) The following transactions shall be exempt from Section 17(a) of the Act:

(1) Transactions solely between a registered investment company and one or more of its fully-owned subsidiaries or solely between two or more fully-owned subsidiaries of such company.

(2) Transactions solely between any subsidiary of a registered investment company and one or more fully-owned subsidiaries of such subsidiary or solely between two or more fully-owned subsidiaries of such subsidiary.

(b) The term "fully-owned subsidiary" as used in this rule, means a subsidiary (1) all of whose outstanding securities, other than directors' qualifying shares, are owned by its parent and/or parent's other fully-owned subsidiaries, and (2) which is not indebted to any person other than its parent and/or the parent's other fully-owned subsidiaries in an amount which is material in relation to the particular subsidiary, excepting (i) indebtedness incurred in the ordinary course of business which is not overdue and which matures within 1 year from the date of its creation, whether evidenced by securities or not, and (ii) any other indebtedness to one or more banks or insurance companies.

Rule 17a-4. Exemption of Transactions Pursuant to Certain Contracts.

Transactions pursuant to a contract shall be exempt from Section 17(a) of the Act if at the time of the making of the contract and for a period of at least 6 months prior thereto no affiliation or other relationship existed which would operate to make such contract or the subsequent performance thereof subject to the provisions of said Section 17(a).

Rule 17a-5. Pro-Rata Distribution Neither "Sale" Nor "Purchase".

When a company makes a pro-rata distribution in cash or in kind among its common stockholders without giving any election to any stockholder as to the specific assets which such stockholder shall receive, such distribution shall not be deemed to involve a sale to or a purchase from such distributing company as those terms are used in Section 17(a) of the Act.

Rule 17a-6. Exemption of Certain Transactions With Affiliates From the Provisions of Paragraphs (1) and (3) of Section 17(a) of the Investment Company Act of 1940.¹

(a) The sale of any security or other property to a registered investment company which is a small business investment company licensed under the Small Business Investment Act of 1958 by an affiliated small business concern, and the borrowing of money or other property from such an investment company by the small business concern, which is prohibited by paragraphs (1) and (3) of Section 17(a) of the Act solely because of an affiliation created through the owning, holding, or controlling with power to vote, directly or indirectly, by the investment company, of voting securities of such concern, shall be exempt from the provisions of said paragraphs. The exemption provided by this rule shall not be available if any person having an affiliate, promoter or principal underwriter relationship with the investment company also has a direct or indirect financial interest in the small business concern. In determining compliance with the preceding sentence, a financial interest in the small business concern shall be disregarded if it represents solely an interest: (i) by a wholly-owned subsidiary of the investment company; (ii) in fees paid for services as a director of the small business concern; (iii) based solely upon ownership of securities of the investment company; or (iv) excepted from the requirements of Rule 17d-1 by paragraph (d) (3) thereof.

(b) The pertinent details of each transaction for which exemption is claimed pursuant to paragraph (a) of this rule shall be reported in writing by the investment company to (i) its stockholders in its annual report to stockholders which report shall cover all such transactions during the preceding 12-months' period, and (ii) the Commission within 30 days after the end of each semi-annual accounting period of the investment company which report shall cover all such transactions during the preceding 6-months' period.

Rule 17d-1. Application Regarding Joint Enterprises or Arrangements and Certain Profit-Sharing Plans.

(a) No affiliated person of or principal underwriter for any registered investment company (other than a company of the character described in Section 12(d) (3) (A) and (B) of the Act) and no affiliated person of such a person or principal underwriter, acting as principal, shall participate in, or effect any transaction in connection with, any joint enterprise or other joint arrangement or profit-sharing plan in which any such registered company, or a company controlled by such registered company, is a participant, and which is entered into, adopted or modified subsequent to the effective date of this rule, unless an application regarding such joint enterprise, arrangement or profit-sharing plan has been filed with the Commission and has been granted by an order entered prior to the submission of such plan or modification to security holders for approval, or prior to such adoption or modification if not so submitted, except that the provisions of this rule shall not preclude any affiliated person from acting as manager of any underwriting syndicate or other group in which such registered or controlled company is a participant and receiving compensation therefor.

(b) In passing upon such applications, the Commission will consider whether the participation of such registered or controlled company in such joint enterprise, joint arrangement or profit-sharing plan on the basis proposed is consistent with the provisions, policies and purposes of the Act and the extent to which such participation is on a basis different from or less advantageous than that of other participants.

(c) "Joint enterprise or other joint arrangement or profit-sharing plan" as used in this rule shall mean any written or oral plan, contract, authorization or arrangement, or any practice or understanding concerning an enterprise or undertaking whereby a registered investment company or a controlled company thereof and any affiliated person of or a principal underwriter for such registered investment company, or any affiliated person of such a person or principal under-

¹ Applicable only to small business investment companies licensed under the Small Business Investment Act of 1958.

writer, have a joint or a joint and several participation, or share in the profits of such enterprise or undertaking, but shall not include an investment advisory contract subject to Section 15 of the Act.

(d) Notwithstanding the requirements of paragraph (a) above, no application need be filed pursuant to this rule with respect to any of the following:

(1) Any profit-sharing plan provided by any controlled company which is not an investment company for its officers or employees, provided no affiliated person of any investment company which is an affiliated person of such controlled company participates therein.

(2) Any plan provided by any registered investment company or any controlled company for its officers or employees if such plan has been qualified under Section 401 of the Internal Revenue Code of 1954 and all contributions paid under said plan by the employers qualify as deductible under Section 404 of said Code.

(3) Any loan or advance of credit to, or acquisition of securities or other property of, a small business concern, or any agreement to do any of the foregoing, ("Investments") made by a bank and a small business investment company (SBIC) licensed under the Small Business Investment Act of 1958, whether such transactions are contemporaneous or separated in time, where the bank is an affiliated person of either (i) the SBIC or (ii) an affiliated person of the SBIC; but reports containing pertinent details as to investments and transactions relating thereto shall be made at such time, on such forms and by such persons as the Commission may from time to time prescribe.²

Rule 17d-2. Form for Report by Small Business Investment Company and Affiliated Bank.

Form N-17D-1 is hereby prescribed as the form for reports required by paragraph (d) (3) of Rule 17d-1.

Rule 17e-1. Remuneration Permitted Affiliated Persons of Registered Investment Companies Acting as Brokers in Over-the-Counter Transactions.

The commission, fee or other remuneration from any source of any person subject to Section 17 (e) of the Act for acting as broker in connection with any sale referred to in paragraph (2) (C) thereof may exceed 1 percent of the sale price of the securities sold if such remuneration does not exceed:

(a) in the case of securities which are listed or admitted to unlisted trading privileges on one or more national securities exchanges, the lowest broker's commission which any exchange upon which the securities are traded fixes as a minimum for effecting such a transaction on such exchange, or

(b) in the case of securities which are not listed or admitted to unlisted trading privileges on any national securities exchange, the lowest broker's commission which is fixed as a minimum for effecting a transaction in listed securities of a similar type, of an equal number of units and at the same price on any national securities exchange located in the same city as the principal office of the broker, or if there is no such exchange located in that city, then on any national securities exchange located in the nearest city where a national securities exchange is located; provided that where a broker represents both purchaser and seller in the same transaction, the remuneration shall not be greater than the minimum commission prescribed by the appropriate exchange for either a purchase or a sale.

* * * * *

Rules Under Section 20

Rule 20a-1. Solicitation of Proxies, Consents and Authorizations.

(a) No person shall solicit or permit the use of his name to solicit any proxy, consent or authorization in respect of any security of which a registered investment company is the issuer, except upon compliance with Rules 20a-2 and 20a-3 and all rules and regulations adopted pursuant to Section 14(a) of the Securities Exchange Act of 1934 that would be applicable to such solicitation if it were made in respect of a security registered on a national securities exchange. Unless the solicitation is made in respect of a security registered on a

² Applicable only to small business investment companies licensed under the Small Business Investment Act of 1958.

national securities exchange, none of the soliciting material need be filed with such exchange.

(b) If the solicitation is made by or on behalf of the management of the investment company, then the investment adviser or any prospective investment adviser and any affiliated person thereof as to whom information is required in the solicitation shall upon request of the investment company promptly transmit to the investment company all information necessary to enable the management of such company to comply with the rules and regulations applicable to such solicitation. If the solicitation is made by any person other than the management of the investment company, on behalf of and with the consent of the investment adviser or prospective investment adviser, then the investment adviser or prospective investment adviser and any affiliated person thereof as to whom information is required in the solicitation shall upon request of the person making the solicitation promptly transmit to such person all information necessary to enable such person to comply with the rules and regulations applicable to the solicitation.

Rule 20a-2. Information Pertaining to Investment Adviser and Investment Advisory Contract.

(a) If action is to be taken with respect to the election of directors of the investment company and the solicitation is made by or on behalf of the management of the investment company or by or on behalf of an investment adviser, the following information shall also be included in the proxy statement.

Instruction.—Information with respect to a prospective investment adviser shall be furnished to the extent applicable.

(1) State the name and address of the investment adviser, the date of the existing investment advisory contract, the date on which it was last submitted to a vote of security holders of the investment company and the purpose of such submission. Briefly describe the terms of the contract, including the rate of compensation of the investment adviser. State the aggregate amount of the investment adviser's fee and the amount and purpose of any other material payments by the investment company to the investment adviser during the last fiscal year of the investment company. If any person is acting as an investment adviser of the investment company otherwise than pursuant to a written contract which has been approved by the security holders of such company, identify such person and describe the nature of the services and arrangements therefor.

(2) State the name, address and principal occupation of the principal executive officer and each director or general partner of the investment adviser.

(3) State the names and addresses of all parents of the investment advisers and show the basis of control of the investment adviser and each parent by its immediate parent.

Instructions.—1. If any person named is a corporation, include the percentage of its voting securities owned by its immediate parent.

2. If any person named is a partnership, the general partners having the three largest partnership interests (computed by whatever method is appropriate in the particular case) shall be named.

(4) If the investment adviser is a corporation and if, to the knowledge of the persons making the solicitation or the persons on whose behalf the solicitation is made, any person not named in answer to subparagraph (3) owns of record or beneficially 10 per cent or more of the outstanding voting securities of the investment adviser, indicate that fact and state the name and address of each such person.

(5) Name each officer, director or nominee for election as a director of the investment company who is an officer, employee, director or general partner of the investment adviser. As to any officer, director or nominee for election as a director of the investment company who is not a director or general partner of the investment adviser and who owns any securities of or has any other material direct or indirect interest in the investment adviser or any person controlling, controlled by or under common control with the investment adviser, state the nature of such interest.

(6) Describe any action with respect to the investment advisory contract which has been taken since the beginning of the last fiscal year by the board of directors of the investment company, unless such action was described in the proxy statement for the last annual meeting for the election of directors. Identify any director of the investment company who, at the time of the action described, owned any securities of, or had any other material direct or indirect interest

in, the investment adviser or any persons controlling, controlled by or under common control with the investment adviser, and state the nature of such interest.

(7) Name each person employed as a broker by or on behalf of the investment company in which the investment adviser, any officer, director or general partner, any person controlling, controlled by or under common control with the investment adviser, or any officer, director or nominee for election as a director of the investment company has any material direct or indirect interest. State the nature of such interest and amount of brokerage fees received by or participated in by each such broker from business originating with the investment company during its last fiscal year.

(8) If any officer, director or any nominee for election as a director of the investment company, any investment adviser, or any person named in response to subparagraph (2) or (3) purchased or sold any securities of the investment adviser or any of its parents, subsequent to the beginning of the last fiscal year of the investment company or is a party to any contract for the purchase or sale of any such securities, describe the transaction, identify the parties, state the consideration, the terms of payment and describe any arrangement or understanding with respect to the composition of the board of directors of the investment company or of the investment adviser, or with respect to the selection or appointment of any person to any office with either such company.

Instruction.—Transactions involving securities in an amount not exceeding 1 per cent of the outstanding securities of any class of the investment adviser or any of its parents may be omitted.

(9) Unless the investment adviser is a bank, include a balance sheet of the investment adviser as of the end of its last fiscal year. Such balance sheet shall be certified by an independent public or certified public accountant. The Commission for good cause shown may, however, in its discretion permit (i) the omission of certification of such balance sheet, or (ii) the summarization or omission of such balance sheet if the investment adviser is primarily engaged in a business or businesses other than the underwriting or distribution of investment company securities or the performance of advisory services for registered investment companies.

(10) If, since the beginning of the investment company's last fiscal year, any investment advisory contract was terminated for any reason, state the date of such termination, identify the investment adviser and describe the circumstances of such termination.

(11) Identify any officer, director or nominee for election as a director of the investment company having any material direct or indirect interest in the principal underwriter or prospective principal underwriter of the securities of the investment company and state the nature of such interest. Describe the nature of any material relationship between the investment adviser and such principal underwriter.

(12) State the names and addresses of all parents of the principal underwriter or prospective principal underwriter of the securities of the investment company, showing the basis of control of such underwriter and each parent by its immediate parent.

Instruction.—The instructions to subparagraph (3) above shall apply to subparagraph (12).

(b) If action is to be taken with respect to an investment advisory contract, the following information shall be included in the proxy statement:

(1) The information specified in subparagraphs (1) through (12) of paragraph (a) shall be included. This information shall be furnished with respect to the existing investment adviser or any prospective investment adviser, whichever is appropriate.

(2) Describe (i) the nature of the action to be taken and the reasons therefore; (ii) the terms of the contract to be acted upon and any material differences between such contract and the arrangements then or previously existing; and (iii) if the action is to be taken because of the termination or prospective termination of a prior or existing contract, the circumstances giving rise to such termination.

(3) Describe any arrangement or understanding made in connection with the proposed investment advisory contract with respect to the composition of the board of directors of the investment company or the investment adviser or with respect to the selection or appointment of any person to any office with either such company.

(4) If the investment adviser acts as such with respect to any other investment company, identify and state the size of each such other company and state the rate of the investment adviser's compensation.

(c) The definitions in Rule 8b-2 shall be applicable to the terms used in this rule.

Rule 20a-3. Information as to Certain Transactions.

(a) This rule shall apply to a solicitation if (i) the information specified in Item 7 of Schedule 14A of Regulation 14 is required to be furnished for an investment company, or (ii) action is to be taken with respect to an investment advisory contract.

(b) Describe briefly, and where practicable, state the approximate amount of any material interest, direct or indirect, of any officer, director or nominee for election as a director of the investment company in any material transactions since the beginning of the investment company's last fiscal year, or in any material proposed transactions, to which the investment adviser of the investment company or any parent or subsidiary of the investment adviser was or is to be a party.

Instructions.—1. Include the name of each person whose interest in any transaction is described and the nature of the relationship by reason of which such interest is required to be described. Where it is not practicable to state the approximate amount of the interest, the approximate amount involved in the transaction shall be indicated.

2. As to any transaction involving the purchase or sale of assets by or to the investment adviser, state the cost of the assets to the purchaser and the cost thereof to the seller if acquired by the seller within 2 years prior to the transaction.

3. If the interest of any person arises from the position of such person as a partner in a partnership, the proportionate interest of such person in transactions to which the partnership is a party need not be set forth but the amount involved in the transaction with the partnership shall be stated.

4. No information need be given in response to this rule with respect to any interest of (i) the investment adviser of the investment company, (ii) any affiliated person of such investment adviser or (iii) of any person whose sole interest is as a security holder of the investment adviser, in any transaction which is not related to the business or operations of the investment company and to which neither the investment company nor any of its parents or subsidiaries is a party.

5. This rule does not require the disclosure of any interest in any transaction unless such interest and transaction are material.

* * * * *

Rules Under Section 30

Rule 30a-1. Annual Reports.

(a) Every registered investment company shall file an annual report, on the appropriate form prescribed therefor, not more than 120 days after the close of each fiscal year ending on or after the date upon which such company files its registration statement pursuant to Section 8(b) : in case the registrant finds it impracticable to file the report within such 120 days, it may file with the Commission an application for an extension of time to a specified date within 6 months after the close of the fiscal year. Such application shall state the grounds of impracticability and shall contain an agreement to file the reports on or before such specified date. The application shall be deemed granted unless the Commission within 10 days after receipt thereof shall enter an order denying the application as being unreasonable and unnecessary under the circumstances.

(b) Every registered investment company shall be exempt from the provisions of Section 30(a) insofar as such section requires the filing of an annual report for any fiscal year ending prior to the date upon which such company files its registration statement pursuant to Section 8(b).

* * * * *

Rule 30b1-1. Form for Quarterly Report of Registered Investment Companies.

The following form is hereby prescribed as the form for quarterly report which shall be filed by registered investment companies, pursuant to Section 30(b) (1) of the Act :

Form N-30B-1 for Registered Management Investment Companies.—This form shall be used by all registered management investment companies except those which issue periodic payment plan certificates.

* * * * *

Rule 30b2-1. Filing of Copies of Reports to Stockholders.

Four copies of every periodic or interim report or similar communication containing financial statements and transmitted by or on behalf of any registered investment company to any class of such company's security holders shall be filed with the Commission not later than 10 days after such transmission.

Rule 30d-1. Reports to Stockholders of Management Companies.

(a) At least semi-annually every registered management company shall transmit by mail, postage prepaid, to each stockholder of record, a report containing all the information and financial statements, or their equivalent, specified in clauses (1) to (6) inclusive of Section 30(d) of the Act. The first such report shall be made as of a date not later than the close of the fiscal year or half-year first occurring on or after December 31, 1940. Each report shall be mailed within 30 days after the date as of which the report is made; except that if the reporting company is a non-diversified company having one or more majority-owned subsidiaries which are not investment companies, the report may be mailed within 60 days after the date as of which it is made, or within such longer period of time as the Commission may permit by order upon application.

(b) Reports made as of the close of the reporting company's fiscal year shall cover the whole fiscal year. Reports made as of any date other than the close of the fiscal year shall cover a period commencing either (1) with the beginning of the fiscal year or (2) with a date not later than the day after the close of the period covered by the last report conforming with the requirements of Section 30(d) of the Act and the rules and regulations thereunder.

(c) The list showing the amounts and values of securities owned on the date of the balance sheet or its equivalent, required by clause (2) of Section 30(d) of the Act, shall indicate each issue separately; except that—

(1) securities which, because believed worthless, have been charged off on the books or written down to a merely nominal carrying amount may be omitted, provided that all securities charged off or written down since the effective date of the Act shall be separately listed in the next succeeding report conforming with the requirements of Section 30(d) and the rules and regulations thereunder, and also, if such next succeeding report is not an annual report, in the next succeeding annual report; and

(2) an amount not exceeding 5 percent of the aggregate value of securities shown on the list may be listed in one amount as "miscellaneous securities," if the securities so listed have been held for not more than one year prior to the date of the balance sheet or its equivalent and have not previously been reported by name in any report or statement transmitted to stockholders or filed with the Commission or with any national securities exchange.

(d) In making reports required under Section 30(d) of the Act, an open-end company may include therein, as the equivalent of the balance sheet required by clause (1) of said section and the statement of surplus required by clause

(4) thereof, the following:

(1) A statement of its assets (showing its investments at "value", as defined in Section 2(a)(39)(B) of the Act) and its liabilities, and of its net assets, and the number and par value or stated value of the shares representing such net assets, all as of the end of the period for which the report is made.

(2) A statement of changes in net assets for the period for which the report is made, showing the net assets (on the same basis of value) as of the beginning of the period, and the various credits and debits resulting in the net assets figure shown pursuant to subparagraph (1) of this paragraph. Each charge which represents more than 5 percent of the total charges during the period and each credit which represents more than 5 percent of the total credits during the period must appear as a separate item.

(3) A statement with respect to the period for which the report is made and with respect to the three complete fiscal years next preceding the commencement of such period, of the net asset value per share (on the same basis of value) of the reporting company's securities at the beginning and at the end of each such period, and a statement of the dividends declared per share during each such period together with the amount per share of such dividends declared out of sources other than net income for each such period, excluding from such net income profits or losses realized on the sale of securities or other properties.

Senator PROXMIRE. Our last witness this morning is Jim Howard, who is the president of the National Association of Small Business Investment Companies. He has been a witness before this committee, a very fine witness, very often in the past.

We are very happy to have you.

STATEMENT OF JAMES W. HOWARD, PRESIDENT, NATIONAL ASSOCIATION OF SMALL BUSINESS INVESTMENT COMPANIES AND PRESIDENT OF GROWTH CAPITAL, INC., CLEVELAND, OHIO

Mr. HOWARD. Thank you, Mr. Chairman.

Mr. Chairman and members of the subcommittee, I appreciate the opportunity to appear once again before this subcommittee, even though I must confess that I regret that the mission is such a negative one.

I would like to depart from my prepared statement because of the prior discussions and points raised by previous witnesses. I would like to elaborate on at least two of the points raised. I am not an attorney, although I believe that over the last several years, I have about had to become one in order to operate an SBIC. Essentially, we are perhaps the most regulated industry in existence, far more than any other type of financial institution. Although I am not an attorney, I have been a debater and I recognize the fact that the first rule of debate is to define your terms. I believe this is pointed out by a letter I received last week—Senator Young's newsletter. In it he commented that a constituent had called a Member of Congress asking for a lady who worked in the office, and the reply that she received to the telephone call was, "I am sorry, she is not here; she is down on the floor with the Congressman."

Well, the constituent was very shocked, because, to her, down on the floor had a completely different connotation than what it has to people here in Washington.

Essentially, I believe this is part of the problem we have with the term "self-dealing." When a person discusses self-dealing, he is likely to be traversing an area where angels fear to tread, for the term carries within itself an innate animadversion. Thus, the witness who points out that there are two sides to this question goes into the fray apparently stripped of his moral armor.

First, I would like to comment my experience with newspapers is different from Mr. Whitney. There was at least one material misstatement in the Wall Street Journal article. That was the statement that SEC had never approved self-dealing transactions. This is far from true; they have approved hundreds over the years under the 1940 act, the Investment Company Act of 1940.

I think, also, that the amount of disclosure required there is far greater and does have a very disastrous effect on the small business concerns involved. I would like to read from the Federal Register, and, incidentally, SEC cases involving self-dealing are published in the Federal Register. Summaries are also published in the SEC Newsletter which is distributed widely across the country. Therefore, the information regarding transactions and applications for approval under section 17 or any other section of the 1940 act does receive wide

publicity. This case is dated August 6, 1963, and appears on page 8265, Saturday, August 10, 1963, Federal Register:

Notice is hereby given that Greater Washington Industrial Investments, Inc. (applicant), 1725 K Street, Northwest, Washington 6, D.C., a District of Columbia corporation licensed under the Small Business Investment Act of 1958 and a closed-end, non-diversified management investment company has filed an application under Section 17(b) of the Investment Company Act for an order exempting from the provisions of Sections 17(a)(1) and 17(a)(2) of the Act, the proposed amendment of the loan agreement between applicant and S. J. Tesauro & Company, Inc. ("Tesauro"), a Michigan corporation, and a small business concern as defined by the Small Business Administration for purposes of the SBI Act. All interested persons are referred to the application filed with the Commission for a full statement of applicant's representations which are summarized below.

On August 30, 1961, applicant and Tesauro entered into a loan agreement under which applicant agreed to purchase at principal amount, an aggregate of two hundred thousand dollars (\$200,000) principal amount of 8 percent convertible debentures of Tesauro to be due 5 years from date of issuance, as follows:

(a) One hundred thousand dollars on the signing of the agreement.

(b) One hundred thousand dollars prior to December 31, 1962 in minimum increments of twenty-five thousand dollars.

Applicant purchased \$100,000 principal amount of debentures on August 31, 1961 and \$100,000 principal amount on December 1, 1961.

Said agreement and the debentures issued thereunder provide for an option in the debenture holder to convert all or part of the debentures, at any time within five years from date of issuance, into Tesauro's Class B (voting) common stock at the rate of one share for each \$5 principal amount of debentures. If all the debentures are converted, applicant will have a 28 percent equity interest in Tesauro. Samuel J. Tesauro, President of Tesauro, has given his personal guarantee for repayment of said debentures. Tesauro is primarily engaged in the business of data processing, advertising and direct mail service.

On November 26, 1962, applicant agreed to subordinate its Tesauro debenture holdings to loans to Tesauro by the National Bank of Detroit in the amount of approximately \$20,000. Said Bank, which had been supplying short-term credit for Tesauro's day to day cash needs, has recently curtailed such credit and is requiring full repayment of existing loans. As a result of such curtailment Tesauro has made arrangements for substitute short-term credit with James Talcott Inc. ("Talcott"), a commercial financing institution, subject to applicant and Tesauro's entering into an agreement whereby Tesauro's \$200,000 debenture now held by applicant, will be subordinated to up to \$100,000 of loans advanced by said Talcott.

Applicant states that it is advised and believes that Tesauro will find it difficult or impossible to survive if it does not obtain immediate short-term credit and that such credit cannot be obtained unless the proposed agreement is entered into immediately. Recent operations of Tesauro have been profitable and applicant represents that there appears to be no other satisfactory way to help safeguard and enhance the value of applicant's investment.

Applicant also states that to the best of its knowledge, no officer, director, employee or five percent shareholder of applicant has any interest, direct or indirect, in Tesauro or in the subject amendments.

The loan agreement between Tesauro and applicant provides that Tesauro will exercise its best efforts to cause the election to the Board of Directors of such person as may from time to time be designated by applicant. Applicant has exercised the right so provided by placing one nominee on the five member board of directors of Tesauro. In view of this, applicant may be deemed to hold five percent or more of the outstanding voting securities of Tesauro, and Tesauro and applicant may be affiliated persons. The amendment to the loan agreement between such affiliated persons may involve a purchase and sale of securities by Tesauro subject to the provisions of Sections 17(a)(1) and 17(a)(2) of the Act and the rules thereunder.

Section 17(a)(1) and Section 17(a)(2) of the Act, as here pertinent, prohibit an affiliated person of a registered investment company from selling to or purchasing from such registered company securities or property, unless the Commission upon application pursuant to Section 17(b), grants an exemption from such provisions upon a finding that the terms of the proposed transaction,

including the consideration to be paid, are reasonable and fair and do not involve overreaching on the part of any person concerned, that the proposed transaction is consistent with the policy of each registered investment company concerned, as recited in its registration statement and reports filed under the Act, and is consistent with the general purposes of the Act.

Notice is further given that any interested person may, not later than August 22, 1963, at 5:30 p.m. submit to the Commission in writing a request for a hearing on the matter accompanied by a statement as to the nature of his interest, the reason for such request and the issues of fact or law proposed to be controverted, or he may request that he be notified if the Commission shall order a hearing thereon. Any such communication should be addressed: Secretary, Securities and Exchange Commission, Washington, D.C., 20549. A copy of such request shall be served personally or by mail (air mail if the person being served is located more than 500 miles from the point of mailing) upon applicant at the address set forth above. Proof of such service (by affidavit or in case of an attorney-at-law by certificate) shall be filed contemporaneously with the request. At any time after said date, as provided by Rule 0-5 of the rules and regulations promulgated under the Act, an order disposing of the application herein may be issued by the Commission upon the basis of the showing contained in said application, unless an order for hearing upon said application shall be issued upon request or upon the Commission's own motion.

It is ordered, That the Secretary of the Commission shall give notice of the filing of this application by mailing a copy of this notice by registered mail to the applicant and to the Director, Office of Investment, Small Business Administration, Washington, D.C., 20416; that notice to all other persons shall also be given by publication of this Notice in the Federal Register; and that a general release of this Commission in respect of this Notice be distributed to the press and mailed to the mailing list for releases.

For the Commission (pursuant to delegated authority).

ORVAL L. DUBOIS, *Secretary*.

I cite this case as an illustration of self-dealing under the 1940 act. It is not self-dealing under SBA's current regulations. The 1940 act defines transactions with affiliates, and a small business concern automatically becomes an affiliate according to the assumed facts as herein stated, where the small business concern has the right to elect a director to the board of that company. They do not have to do so, but if they have a right to elect a director, or to nominate a director for election, SEC says they are affiliates.

Therefore self-dealing, under the 1940 act, has much broader implications and restrictions than it does under SBA's regulations. This transaction would probably not be subject to SBA approval, but did require approval of SEC.

Any material change in a loan agreement of an affiliate requires an order from SEC. For example, in this instance, where there was a change of subordination from a bank to a finance company, it took the SBIC about 2 months to get such approval. I understand that the small business concern was very adversely affected. They have had a difficult time getting orders because of their precarious financial position, which has been publicly revealed, as a result of the SBIC's request for an order. This is not true for their competitors, even though their competitors may be even worse off. No other financial institution reveals information of this nature about its loans and clients.

Now, I am sure that most of you, if you had borrowed money, would be very reluctant to have the bank reveal the fact that you have x dollars borrowed from the bank at 6 percent and the bank has had to extend the loan for 5 years, because you couldn't pay it. Also that you are delinquent on your interest. The transaction may also only involve a few changes in your loan. Yet this is what these small

business concerns are being asked to do. A small businessman historically is the kind of person who creates a business, who goes into business for himself, has a great deal of independence. He wants to be independent. He goes to a SBIC with some reluctance, because he knows that most SBIC's are going to require an equity interest. He is very jealous of revealing facts about his company to the public at large and particularly where competitors can get such information. So disclosure and the amount of such disclosure is a material fact as far as the small business applicant is concerned.

Senator PROXMIRE. You say disclosure and amount of such disclosure. Supposing the disclosure is confined to what we propose as one of the alternatives, that is, the affiliation of the borrower and also the terms of the loan, and not the product and all the rest, that you indicate here has been so damaging. What is the matter with that kind of disclosure?

Mr. HOWARD. The basic problem, Mr. Chairman, is that it is rather like the camel putting his head under the tent; you never know where he is going to stop.

Senator PROXMIRE. We stop in the law, and just say this is all that is required.

Mr. HOWARD. I can speak with a great deal of experience, sir, that laws can be changed. We had a law passed in 1958 that purported to do certain things and under which we were permitted to operate and make investments up to 20 percent of our capital and surplus. That is not the case today. There are many other restrictions that have been made involving material changes in the program. The ground rules have been drastically altered since most of us were licensed.

Senator PROXMIRE. An overwhelming majority of SBIC's are not affected by the limitation and that limitation is probably going to be eliminated, unfortunately.

Mr. HOWARD. We certainly hope the committee—

Senator PROXMIRE. I am for the Proxmire amendment; I am probably a minority.

Mr. HOWARD. We were also for the Proxmire bill, sir, and I personally thought it was an excellent bill. I refer to the bill when the act was expanded, to permit SBIC's to invest in other securities. The Proxmire amendment, I always have been against, as you know. However, conceding an outright prohibition would affect less than 2 percent, and this is distorted somewhat. I go back to the question of how you define self-dealing transactions. Is any transaction with an affiliate self-dealing? If you use the definition of self-dealing and affiliate, as defined by the 1940 act, you get into much broader areas, and the amount of disclosure to be pertinent would have to be far more revealing. If you use, for the moment, we will say, that definition of self-dealing, then, as I see it, you could possibly raise problems where an SBIC made an investment in a company, and elected a man to the board, or merely nominated a man for election to the board of directors of that small business. If the small business then needed additional funds, again there would be the problem of disclosure and prior approval, simply by virtue of the fact that a self-dealing transaction came about because the director of the company was put on by the SBIC or nominated by the SBIC. It might be a staff member of the

SBIC or a director of the SBIC. This is very common. The first investment would not be self-dealing, but the second would by virtue of the fact the SBIC was trying to exercise good judgment in superintending and watching its investment and had placed a director on the board of the borrower.

Senator PROXMIRE. The proposed policy of the SBA on self-dealing is simply a partial disclosure policy.

Mr. HOWARD. Why should additional requirements and restrictions be imposed on a small business simply because the SBIC was trying to protect its investment and was acting in the interests of the SBIC's shareholders by having a director on the board of the small business borrower?

Senator PROXMIRE. The reason for it, of course, is so that there will be some public scrutiny and some opportunity to regulate this without having complete reliance on a Washington office, which can't possibly provide the kind of regulation which some public knowledge at least, of the transactions, accurate knowledge, would provide.

Mr. HOWARD. What you are doing then is to require the resignation of a director.

Senator PROXMIRE. No, no; all you are requiring is people know what is going on.

Mr. HOWARD. No; the practical effect, Mr. Chairman, would be that the SBIC would not put a director on the board of the small business concern and neither—

Senator PROXMIRE. I don't say, and I don't think anybody has said, that there is any evil about a self-dealing operation, necessarily. I agree with the Senator from Colorado when he says they are not necessarily wrong. I would say the overwhelming majority of such loans are right, good, and necessary and desirable, but what I say is there is no reason in the world why they shouldn't be known, shouldn't be public. If there is something wrong about it, then I think they are less likely to be done if it is known that they have to be made public.

Mr. HOWARD. You have to look at the transaction and regulations involving SBIC's and the overall umbrella of restrictions under which SBIC's are required to operate. Every time you add more restrictions on the operations of the business of lending money by the SBIC and superintending of its investments, you tend to discourage borrowers. Now I have been told that in the Washington area, as a result of the wide publicity that this transaction has received and others of a similar nature, that many companies who might otherwise go to SBIC's are no longer interested in seeking financing from SBIC's, because of the delay and disclosure required, if they run into problems. Their attorneys are advising them not to go to SBIC's, because things that today are confidential information might tomorrow become public information by virtue of transactions and disclosure such as I have outlined here.

Senator PROXMIRE. Mr. Howard, these are just strawmen. We are not asking for confidential information, all we are asking for is the identity of the person who is getting the loan, his affiliation with the SBIC, and the terms of the loan disclosed. I don't think we are going to press for the exact requirements of the Investment Act of 1940 be adopted for all SBIC's. There is no intention to do that. What we are proposing, I think, most of us are interested in providing

for very limited disclosure and that is all. Now you can say that if we require every little SBIC to come in under the Investment Act of 1940, that it is going to be a serious problem for them, I couldn't agree with you more and there wouldn't be a chance of getting that out of subcommittee and I don't think there would be a vote for it.

Mr. HOWARD. I believe, in any definition you use as far as self-dealing is concerned, that the current regulations, with the modifications suggested by Mr. Foley, are more than adequate to cover the problem, if in fact there is a problem. I say again, that with the changes and the adverse publicity that the industry has received, if further restrictions are piled upon the existing restrictions, it will tend to adversely affect the industry. If the result is there are no SBIC's, then small business concerns who need financing will have been materially injured.

Senator PROXMIRE. You see the difficulty is that nothing would hurt this industry more, both with the public and especially with Congress, than some scandals that have involved self-dealing that discourage the public and the investing public from getting involved in SBIC's. You could have the same kind of situation here as we had with the Reconstruction Finance Corporation if we have this kind of scandal development. I feel that the best protection and insurance the SBIC's can have and the Congress can have and the public can have is to have at least a limited amount of disclosure so that we know what is going on. As Senator Dominick said earlier, it is pretty much of an insurance policy. He said that in a different regard, but, if you disclose what the situation is, you are in a much better position than you are if it is concealed, and then the scandal develops.

Mr. HOWARD. The basic disclosure policy followed by IRS, I believe, is a good one, again going back to the particular problem of small business concerns. The SEC adopted some time back a rule that would keep the name of the small business concern secret, if the small business investment company so requested at the time they filed the initial material on the small business concern. This is an existing rule and we feel it is a good one. Unfortunately, the SBIC must start with it being secret right from their first filing, because as I understand it, if the SBIC requests that the name be kept secret on subsequent filings, SEC won't do it. However, if the SBIC initially keeps the name secret, then it can continue to do so.

The rule proposed by Mr. Foley would give all of the facts, perhaps even more facts than what you are asking, but would keep the name of the company secret. I believe the name of the company is immaterial; it is the facts that are material and speak for themselves.

Senator PROXMIRE. Maybe the facts speak for themselves, but who is going to go through that? It is not going to be made available in the area where there is an interest, banking interest, or competitive interest, or public interest, or employee interest, or a stockholder interest, where somebody is going to say, "Well, now, I want to know about this; maybe there is something wrong." The SBA would make anonymous information available, but I am sure the SBA isn't going to tell us they would like to send the information into every single community so it could be published and printed throughout the country. It seems to me the efficient way is to have this information made available in a newspaper and in the community where the transaction takes place. Otherwise, the so-called disclosure in which the borrower

is anonymous, nobody knows who you are talking about, and the location is not revealed, we don't know where it is, does mean very much.

Mr. HOWARD. To me the facts of the matter are the most important, not the name. If a guy murders another man, the fact that a murder was committed is the important thing, not the fact the guy who was murdered was John Doe or Helen Roe.

Senator PROXMIRE. You might know a murder is committed, but until you catch the murderer you are not really able to do anything about it or protect the public or prevent the murderer from repeating his crime.

Mr. HOWARD. Justice should be applied equally regardless of the name involved or the parties involved. That is my point.

To go on, I trust that the phrase "self-dealing" will not blind Congress to the true issues at stake.

First, let us make our frame of reference explicit. One part of SBA's regulations says that "self-dealing to the prejudice of SBA or the licensee's shareholders is prohibited" (107.706(a)). The National Association of Small Business Investment Companies is in complete agreement with that regulation and believes that any SBIC or any of its officers found in violation of it should be thrown out of the program and prosecuted.

We, however, would go even further. The code of ethics of NASBIC, voluntarily subscribed to by a great majority of all licensees, says that "the constant goal of each SBIC shall be to improve the welfare of the small business concerns which it serves." Therefore, to the extent of our ability to do so, we would penalize those SBIC's which act adversely to the best interests of the small business concern as well as those over-reaching to the prejudice of SBA or the other stockholders of the SBIC.

Senator DOMINICK. How would you do that?

Mr. HOWARD. By enforcing the code of ethics we have currently, dropping the violator from membership in NASBIC, as far as our industry is concerned. As far as SBA is concerned, they can go all the way up to revoking the license and asking for receiver of the SBIC.

Senator PROXMIRE. The question is how do you know it is taking place until the damage is done and there is no real recourse?

Mr. HOWARD. We do not operate in a vacuum. SBA periodically audits all SBIC's. They make a detailed audit on all transactions with affiliated companies and with small business borrowers. All pertinent material is available to them.

Senator PROXMIRE. But when these self-dealing loans are made, they are made in an atmosphere of one colleague dealing with others, one close business associate dealing with others, one social friend dealing with others; when these are made they are approved by the SBA on the basis of correspondence without on-the-spot audit, without any visit to the community, without any direct inquiry about the situation except what takes place in the exchange of correspondence.

Mr. HOWARD. This is a pattern—

Senator PROXMIRE. We are not saying that you should go much farther, but what we are saying is that some local knowledge should be permitted, so the public can know that this is going on, people involved in it.

Mr. HOWARD. Again, to put the problem in the proper frame of reference, we are dealing with a company that is licensed. First, all officers and directors have to be approved by SBA when the proponent submits its proposed form of operation in a detailed proposal. They have to put up privately at least \$150,000 of their own funds before they can borrow a nickel of Government money. Secondly—

Senator PROXMIRE. Let me just stop there.

A small SBIC—here it seems to me is the real public interest reason why we should require some disclosure or some kind of limitation on this self-dealing, because Government money is involved in these small SBIC's. Taxpayers' money is involved. These are firms that are borrowing from the Federal Government. They have that money involved. These firms that are regulated by and large by the Securities and Exchange Commission don't have a penny of Government money.

Mr. HOWARD. Secondly, let me point out—

Senator PROXMIRE. Some of them do, as Senator Dominick tells me.

Mr. HOWARD. In the small SBIC probably the board of directors will own the majority of the stock, if not all. In many small companies I believe the board of directors own all of the stock—

Senator PROXMIRE. And the really small SBIC, the Government puts up \$2 for every \$1 the local people put up.

Mr. HOWARD. They do under certain restrictions and certain rules. But initially, the people lending that money are dealing with their own money.

Senator PROXMIRE. Dealing with \$2 of Uncle Sam's and \$1 of their own, and make a deal with themselves.

Mr. HOWARD. First, there is a restriction on the size of the investments that can be made by an SBIC. An SBIC can only invest 20 percent of its capital and surplus, except for large companies like ours who have the Proxmire amendment to consider, in any one small business concern.

A small business concern has a definition itself, and affiliated groups are considered in the total. A director on a small business concern could only get one loan of \$60,000, if he is a significant shareholder of the borrower, and if he meets the test and his company that is borrowing is considered to be a separate independent entity. The share holdings and many other factors determine whether the concern is a small business. Therefore, he is limited to borrowing \$60,000. That is the maximum he could borrow, and to do so a group of people who are sitting in judgment on that loan put in \$150,000 of their money. Therefore, I don't see the undue concern for the Government funds involved.

Before the Government loses a penny the small business investors in that small business investment company lose all of their money. They are on the bottom as far as priority of claim goes.

Now, the next point, to go on: NASBIC's code of ethics takes one additional step, too. It says that—

unethical conduct shall be deemed to include any evasive device intended to cloak noncompliance with the act, regulations, or code of ethics.

Therefore, it should be apparent that NASBIC stands fully committed to the prohibition against self-dealing when it is prejudicial to the small business, to the SBA, or to the welfare of the stockholders of the SBIC.

Senator PROXMIRE. I have great regard for NASBIC, and I think you have done a fine job; but NASBIC doesn't have any regulatory power or any penal power. It doesn't mean anything if somebody is kicked out of NASBIC. The biggest SBIC in the country isn't a member of NASBIC. And so, while that is fine, I think that certainly we can't allow a voluntary association that doesn't include all of the SBIC's in it, and which has no real force, and no real ability, to enforce its own code.

There are some very fine associations in the television industry, National Association of Broadcasters, very excellent codes of conduct. But if the Government relied on them it would mean that many TV and radio firms outside of the association would be in a position where they could exploit and take advantage of their positions, as they might do, without FCC regulation.

Mr. HOWARD. We don't profess to represent the biggest and the smallest, but we do profess to represent the best.

Senator PROXMIRE. You represent some excellent ones. You have a fine association. I am just saying we can't rely to any significant extent on a voluntary association code of ethics, as fine as they are, to protect the public or stockholders or Government money that is involved.

Mr. HOWARD. I grant that, and my statement does not imply that.

Furthermore, I am saying that in the framework of SBA's regulations SBA recognizes this second area as distinct from the earlier reference.

Let me state it most simply, since you gentlemen have already received the formal language of the SBA regulations:

An SBIC must get permission from the SBA before it can invest in a small business when someone in a position to influence the decision of the SBIC is also an officer, director, or major stockholder of the small business concern.

NASBIC believes that this regulation is sound. We feel that the agency was on firm ground when it adopted the precedent set by other regulatory bodies and demanded the right to rule on such situations. In an industry where Government loans and other stockholders may be involved, it is proper for the regulator to examine the facts in each case before it grants permission for the loan or the investment to be made.

It should be obvious from my statement that the SBIC industry, as represented in NASBIC, takes no exception to the rules promulgated by the Small Business Administration to deal with questions of self-dealing.

Furthermore, so far as we can tell, the SBA has administered these regulations in an effective and sound manner. I am aware that confirmed cynics and prejudiced peeping toms may believe it significant and unnatural that the sheep and the wolf, the regulated and the regulator, thus lie down together. Nonetheless, I stand by this statement and praise the Small Business Administration for its oft-demonstrated willingness to work with the industry in devising an effective instrument for channeling long-term credit and equity capital to thousands of American small business firms.

As I indicated, the industry has no way to appraise the accuracy of the newspaper article which brought this matter to the attention of

the Small Business Subcommittee. Let me say only that I can guarantee that the SBA has many arrows in its quiver and any SBIC which misinforms or misleads the agency in this or any other matter will soon learn the truth of my assertion to its vast discomfort.

It is for these reasons that Congress can rest assured that the rules covering self-dealing and the administration of those rules will protect the Government, the investor in an SBIC and the small business firm being financed.

May I be indulged in a few other observations?

First, let us realize that we are speaking of only a very small percentage of the total number of SBIC transactions. To generalize from these exceptions and to tar the entire program with such a broad brush would be unwise. Certainly the SBA must study the handful of cases cited in the article and examine them to learn if its administrative techniques are imperfect.

Secondly, we must remember that the SBIC program is essentially a private undertaking. The 1958 act specifically spells out the private nature of the transaction between the SBIC and the borrower. Therefore the regulatory agency must be careful that, in its zeal to restrain wrongdoing, it does not make the SBIC program unworkable. No amount of legislation or regulation deters the true criminal; nonetheless, severe restrictions can seriously harm the innocent.

Senator PROXMIRE. That is an interesting sentence: "No amount of legislation or regulation deters the true criminal." You wouldn't say there shouldn't be any laws against crimes such as theft and murder?

Mr. HOWARD. There are strong movements to remove capital punishment, because the experience of those who have no capital punishment laws—

Senator PROXMIRE. We don't have it in Wisconsin, and I am against it. We have the prompt and very effective punishment taken against murder. I don't mean to detain you, because we have detained you too long; but what you are arguing is no legislation deters the true criminal. Sure it does. You know it does.

Certainly, if a man is a criminal, one of the things he must worry about is whether he is going to get arrested, prosecuted, and jailed, or maybe executed in some States. This deters him. Isn't that correct?

Mr. HOWARD. This is a point that is like a wardroom argument. It is impossible to prove either position.

I think that basically there are some deterrents to a person of certain actions. The point that I am making here is that what you are doing is driving people from coming into SBIC's.

Senator PROXMIRE. No; because the last part of that sentence—"nonetheless severe restrictions can seriously harm the innocent." I agree, we are not asking for severe restrictions. All we are asking is what I say is a very modest, mild, limited disclosure, far less than is required by SEC, far less than is required by others. And in the judgment of these men whose lives are devoted to the SEC, they don't know of any instance where disclosure of the person who is borrowing, or his affiliation with the SBIC, and in no instance, in their judgment, has this had an adverse effect or is it likely to have an adverse effect. The only instance is if some product information will be revealed. We are not asking for that. It is not a severe restriction.

Mr. HOWARD. I would have to disagree strongly with that, Mr. Chairman. I feel in certain instances particularly with regard to SBIC applications, that the restrictions under the 1940 act imposed on public companies, can and have injured the small business concerns.

Senator PROXMIRE. Yes, indeed; that isn't what I am talking about or what they were talking about. They admitted and said there was a case where they had not required disclosure of certain information regarding a mineral, as you recall, but that would have had to be reported ordinarily under the investment act, if it hadn't been for their administration. We are not asking for the investment act, we are asking, as I say, for a very limited application of it.

Mr. HOWARD. Again, you have to start with defining your terms.

With respect to the term "self-dealing"—you could, by improper definition, include many transactions that today are not subject to—

Senator PROXMIRE. I haven't heard a thing in the testimony or anything in the proposed alternatives here that would change the SBA's present definition of "self-dealing." We haven't attacked that, we haven't said that the definition is inadequate or improper or has to be broadened. We are pretty much accepting that. We are discussing how to handle the self-dealing as now defined and you presumably on the basis of your testimony here, would say "self-dealing" as now defined is not oppressive.

Mr. HOWARD. That is right, under SBA's regulations.

Senator PROXMIRE. I don't know of anyone proposing it be broadened.

Mr. HOWARD. My basic point is I feel the law as such, and the regulations issued under that law, as it exists today, covers the problem sufficiently. I think that there has been no abuse of this, and that the authority of SBA currently is broad enough to handle any problems that may arise. They are examining SBIC's. If there was never any examination of the small business investment companies by SBA, then it would be a different matter.

Senator PROXMIRE. But the fact is, while there may be no great scandal—this is a small and growing program; it is brand new, and we hope it will expand greatly—the fact is, that this is the only agency in Government which permits on this broad scale, for all transactions, without limitation, self-dealing, and it has only prevented about 20 percent of those who applied to engage in self-dealing.

That is No. 1, and No. 2, it is the only agency which does not require some degree of disclosure, and the SEC, the big agency which affects most American business requires enormous disclosure, very broad disclosure.

Furthermore, this SBIC program involves a great deal of Government money. The taxpayer's money is involved. We have a responsibility as Senators to protect that money.

Mr. HOWARD. I recognize our responsibility, sir, but actually the facts as you state them are not completely correct. SBA is not the only agency that does not prohibit self-dealing.

Senator PROXMIRE. Wait a minute. I didn't say that; I said "does not have prohibitions against broad aspects of self-dealing."

SEC, as I am sure you would agree, prohibits most self-dealing and it has serious limitations on other kinds of self-dealing, with very rare exceptions.

Mr. HOWARD. Only with a very limited number of investment companies. There are actually only a few companies out of thousands of corporations in this country that are subjected to the requirements of the Investment Company Act of 1940. And it is only those companies from whom this disclosure is required, so there are—

Senator PROXMIRE. Anybody who wants to borrow from the public and has 100 stockholders, which involves the great amount of investment of the American—

Mr. HOWARD. That is not true, that is not true. An investment company—again we have to define our terms—the term “investment company” is a specific definition spelled out in the Investment Company Act of 1940.

Senator PROXMIRE. Now you are talking about something else.

Mr. HOWARD. No; I am not.

Senator PROXMIRE. What I am talking about is the fact if manufacturing firm A in Milwaukee or New Jersey or Pittsburgh or elsewhere wants to borrow money from the American public, wants to issue securities and if it wants to sell publicly and if it is going to sell in a way in which they will have 100 stockholders or so, then it would be necessary, as I understand it, for them to qualify with the Securities and Exchange Commission and they will have to meet certain requirements. It may not be under the Investment Company Act, it may be under the SEC Act, Securities Exchange Act, and it may be under any number of other acts.

Mr. HOWARD. That is completely wrong. The 100 investors or shareholders applies to the definition of an investment company subject to the Investment Company Act of 1940. There are many investment companies that have fewer than 100 shareholders, who are not subject to the Investment Company Act of 1940, and any company who borrows from a bank or borrows from other sources on a private basis does not register its offerings with the Securities and Exchange Commission.

First, all SBIC transactions are made under an exemption of the Securities Act of 1933—at least I will say 99 percent—I believe all—under which on a private placement, a direct private placement, they do not have to register that transaction with the Securities and Exchange Commission. The bulk of all corporate borrowing is made completely independent of the Securities and Exchange Commission without their ever knowing anything about it.

Senator PROXMIRE. We are talking about different things.

Mr. HOWARD. No we are not.

Senator PROXMIRE. You are talking about the bulk of corporate borrowing and, of course, you are right to the extent that it involves commercial banks. A corporation going to a commercial bank, there is no reason in the world why they should have the same disclosure and protective features you have on your borrowing from the public. But, I say, when a firm, for instance, goes on the New York Stock Exchange or the American Exchange or the Midwest Stock Exchange or any other stock exchanges that are operating in the country and raises money from the public where an enormous amount of the funds invested by the public is involved, then there are certain strict restrictions on self-dealing that are involved although no Government money may be involved.

Mr. HOWARD. The same restrictions apply to SBIC's. When we raise our funds from the public through a public offering of securities, we are subject to the 1933 act and so is any other corporation. Now, if the small business concern is borrowing its money on what would constitute a public offering, they are subject to the full requirements of the 1933 act, too. But the bulk of such borrowings are made on a private, negotiated basis with institution lenders such as insurance companies, pension funds, and those are not registered with the Securities and Exchange Commission.

Basically, again, if a bank could not lend funds or make loans to the companies represented on their boards by individuals, they would have a hard time getting directors. In fact, it is very common for a bank to have the chief executive officer or one of the top officers of its major customers on its board. This is done to promote its business, to get deposits, and get loans.

Those transactions are not publicly revealed and so we are dealing with a very, very minute segment of the overall economy. An investor, John Doe, who has money to invest and who is looking for something that is going to put his kids through college or provide a nest egg for him in the future, has thousands of places to invest his funds. John looks at the SBIC industry and sees an industry that has had major changes in its regulation and laws, tremendous amounts of adverse publicity by slanted articles in the Nation's financial press, and by the use of terms that are very misleading such as the term "self-dealing." This investor, when he goes out to invest money, is not going to invest in SBIC's.

Senator PROXMIRE. You see, here you have a combination. In the first place, you have the Government money involved in all the small SBIC's—virtually all. In the big SBIC's, you don't have Government money. There, by and large, you very, very often have more than 100 stockholders and you are among the firms regulated by the Investment Company Act. You do have in addition to Government money involved, stockholders involved, at least to a limited extent, and what I am saying is with this combination that a limited amount of disclosure should not be considered oppressive and it is not a matter of piling one enormous regulatory problem on top of another.

Mr. HOWARD. At some point, that straw broke the camel's back, and it is a question of how many straws a camel can carry. My basic point is that you have to look at the problem in terms of the overall complex of regulations and laws on SBIC's. We have been advised that the Securities and Exchange Commission is considering a possibility of a rule that would further exempt certain transactions under section 17(a)2 between SBIC's registered under the 1940 act and small business concerns.

For example, those restrictions are far more restrictive than what SBA's regulations are on the term "self-dealing" because "self-dealing" to SEC has a much greater and different connotation than it does to SBA.

To finish, again as a corollary to the point above, I caution against any move to impose an absolute legislative or administrative prohibition against self-dealing where no prejudice is involved. I can tell you that this would be a dramatic example of throwing the baby out with the bath, for not only would it deliver a sharp setback to the pro-

gram and those who have invested in it, but it would also most definitely hurt those for whom the program was established—the qualified small business concerns needing dollars.

I can make that statement without any fear of contradiction. To buttress the point, let me give you some concrete examples.

The typical small business which calls upon an SBIC, is a closely held corporation with only one or two or three stockholders, who are also its officers, but ordinarily it has a board of directors consisting of a large number of people. The nonmanagement directors may be the firm's lawyer, its accountant, a banker, or a leading businessman. This is all well and good, since it conforms to the best theoretical principles of the constitution of a board of directors. But here's the rub: These same men are likely to be the people an SBIC tries to get to serve on its board of directors. And when there are common directors, the technical application of self-dealing takes over.

I am certain that all of you have knowledge of a number of businesses in your own communities—and hopefully, you also know of SBIC's which serve your hometowns. From your own experience, then, you can perceive the damage which would be wrought by such an outright prohibition. Obviously, these examples are most numerous in smaller cities and communities.

Furthermore, let me digress here to say that I am aware of no other financial institution which labors under such a handicap. If a bank could not make a loan to any business with which it had common directors, how many businessmen do you think would serve on bank boards? Even publicly owned investment companies which are regulated by the Securities and Exchange Commission under the Investment Act of 1940 have the right to apply to the SEC for approval of transactions between "affiliated person"—or what we could call self-dealing. The SEC, contrary to the implications of the Wall Street Journal article, has approved hundreds of self-dealing transactions.

One final note: It is possible that this subcommittee may consider disclosure as a prerequisite for approval of self-dealing transactions. Although I have not had an opportunity to touch base with all our members—or even all those who serve on NASBIC's board of governors—I have discussed it with our top officers. We would not oppose such a requirement, so long as it did not involve long-drawn-out, complicated, and costly proceedings. This subcommittee recently received testimony that the SEC requires more than 6 months to dispose of some "affiliated persons" proceedings submitted to it. I can tell you that this sort of a time delay is an outright death sentence to the small business client we are trying to help and it would also be a fatal blow to the entire program, in my opinion.

Senator PROXMIRE. Or provided you didn't disclose the name of the firm involved.

Mr. HOWARD. Significant financial information that could be utilized to adverse interests of the small business concern. I can't repeat enough, Mr. Chairman, that when you affect a small business concern, you affect the shareholders of the SBIC who are never going to make a profit if the companies in which we invest don't become profitable. It is a matter of simple economics.

Senator PROXMIRE. I just can't get it through my head why an honorable transaction involving SBIC and its directors has any onus

at all. As long as there is nothing wrong why not reveal it and reveal it to the limited extent we are asking? That is what I cannot understand. I am going to try hard to see your viewpoint, but it is tough to see it because there hasn't been a single concrete example, there hasn't been even any logical generalization indicating why a man who is a director of an SBIC and wants to borrow money from that SBIC, get money from SBIC one way or another for his small business, why he should be adverse to having that fact recognized under the terms of the loan. What is the matter with it?

Mr. HOWARD. The question is how much information do you reveal?

Senator PROXMIRE. Only the borrower and the terms of the loan. That is all we say in our alternative. Let me read that to you. Here is all we require [reads:]

Nature of interest or interests required of giving such notice and the terms upon which the purchase or loan was made.

We don't require information as to why it was a good loan and that kind of thing be made public. We require that be made available to the Administrator as it is now. All we require is the name of the person borrowing and the terms upon which the purchase or loan was made. That is all this major alternative is.

Mr. HOWARD. You don't require legislation to do that.

Senator PROXMIRE. Sure SBA can do it but it hasn't done it to date. Mr. Foley very graciously said he might consider doing it, but if it is right, why not provide it in the law, especially when nobody, even the very articulate and extremely well-informed champion of NASBIC, president of NASBIC, can't give me an argument on why not?

Mr. HOWARD. Senator, I go back to my opening remarks, the question of disclosure and the terms that are put into the law can be interpreted in many different ways.

Senator PROXMIRE. I have given you what we provide and this is awfully limited: "Nature of the interest or interests required of giving such notice and the terms by which the purchase or loan was made." That is pretty limited. If you want to amend it further, we would be very interested in seeing your proposal. The intent at least, as I have said over and over again this morning and this afternoon, is that it would be confined to the identification of the person borrowing the money and his affiliation with the SBIC and the length of the loan, the amount of the loan, the interest rate involved in the loan, and so forth. That is it.

Mr. HOWARD. If it were limited to information that could not be used adversely against the small business concern by its competitors, by others in the industry or large producers who may not be competing with that company now but who might on the basis of certain information being revealed, we would support it. We are not against the principle of disclosure, but the amount of disclosure and the requirements—

Senator PROXMIRE. Might be very onerous to the small businessman, No. 1, and far more important, very damaging if he has to reveal information regarding his product and information regarding research plans and that kind of thing. There is no intention on my part and I don't think any intention on anybody else's part to require anything that would injure any small businessman.

Mr. HOWARD. This is the most important point and again, I think the procedure proposed to be followed by SBA under Mr. Foley's testimony would be a sound and workable approach. He is revealing the facts but not identifying the company.

Senator PROXMIRE. He is not revealing the key fact, who it is and where it is.

Mr. HOWARD. For example, one of the problems connected with this question involves timing. The time required becomes very important. The company that I mentioned earlier and quoted from the Federal Register, I understand took about 2 months. In that instance, that could have been fatal. It was not but certainly it had a tremendously adverse effect.

Senator PROXMIRE. In my judgment, if I were in Mr. Foley's position, I would certainly be for that because I think I would be protected.

You have to be very, very careful. Under the SBA proposal, you know there is not going to be any possibility of having local people make complaints that put you in a position of investigating further and checking it. On the other hand our proposed disclosure, I think, would be very helpful to Mr. Foley and I can't see any reason why it should take a minute longer. It is a very simple fact. The SBA knows it.

Mr. HOWARD. First, we have the problem of getting information. In order to make an adequate decision, they have to have adequate information. This sometimes can take a great deal of time and certainly, the proceedings—

Senator PROXMIRE. We are not requiring one single bit of additional information that they don't have now. All we are requiring is that they disclose a small part of it but no additional information.

Mr. HOWARD. OK; however, this subcommittee recently had testimony that the SEC required in one instance more than 6 months to dispose of some affiliated person's proceedings. This sort of time delay can be an outright death sentence to the small business client that SBIC was trying to help. It could be a fatal blow to the entire program when compounded. Now this probably is not a normal period, but I'm not sure if the transaction that Mr. Salik testified about has been approved yet.

I hope that the Congress will tell SBA to continue scrutinizing self-dealing transactions under its present regulations, but expeditiously, so long as no question of prejudice to the Government's interest or those of other stockholders is involved.

Incidentally, I would remind this subcommittee that it possesses broad powers under section 10 of the Small Business Act to examine and inspect all correspondence, records of inquiries, memorandums, reports, books, and records of the SBA—including the Investment Division. If there is ever any evidence or even any rumors concerning lack of enforcement of the agency's regulations, Congress has the power to investigate. Here again, there is a remedy for any potential ills which seems to me to be preferable to ironbound restrictions which threaten to kill this significant experiment in helping small business.

Gentlemen, the task of trying to make a profit by investing in small businesses is a difficult one. Congress passed the Small Busi-

ness Investment Act of 1958 because it realized that this important task was not being accomplished by existing financial institutions. There was complete recognition that an "equity gap" did exist and SBIC's were authorized to try to fill the void. That mandate we have been attempting to carry out. The passage of S. 298 will give a substantial boost to our efforts. On the other hand, the imposition of further controls, the disqualification of further activities, the rigidities of further prohibitions will all serve to frustrate the purposes of the act and will indicate to private investors that the SBIC program cannot become a profitable, viable financial institution.

I would like to close my testimony by quoting from an article written by Mr. Jules Backman, research professor of economics at New York University on "Economic Forecasts: and Sound Growth," as published in the August issue of the Nation's Business. There is a comment that he has regarding the role of Government that could have been written exactly for our program. It is on page 76.

What Government can do. The Government's main role should be to create the climate which induces the exercise of initiative and risk taking. Such a climate is indispensable because the rate of economic growth reflects myriad private decisions. What are the ingredients for such a climate? We must have confidence that the Government will not interfere excessively and arbitrarily with the economic process and that the rules of the game will not be changed. We must be rewarded for success and thus induced to take the risks which are so widespread in our profit and loss economy.

I think that is a very apt summary of the feeling of NASBIC as to the Government's role with regard to the SBIC programs.

Senator PROXMIRE. That is a fine statement. I subscribe to everything, but I don't think even Mr. Backman would say, if you really asked him, that he doesn't think the rules of the game should ever be changed. After all, we live in a progressive democracy in which we believe that we can learn and improve and gain from experience, and so forth, and on the basis of that experience, change.

The SEC has just had a recommendation that I think may very well eventually result in substantial changes on the basis of very thorough and competent investigation. I think that there may be changes in many areas, and I think you would agree we have to have changes in the rules of the game.

I would agree those changes should be limited, should be modest, and should be only as much as is required and that, I think, is all we want to do with this kind of legislation.

Mr. HOWARD. A process of evolution rather than revolution.

Senator PROXMIRE. Thank you very much for a fine statement. I apologize for keeping you so long but I think you were very stimulating.

Mr. HOWARD. I sincerely hope that the committee will be in a position now to act on S. 298. As you know, we have three bills pending in the Senate.

Senator PROXMIRE. Yes, indeed.

Mr. HOWARD. All of them, we feel in their entirety, are important to the program.

Thank you very much for the opportunity.

(Mr. Howard later supplied the following information for the record:)

NATIONAL ASSOCIATION OF
SMALL BUSINESS INVESTMENT COMPANIES,
Washington, D.C., September 12, 1963.

HON. WILLIAM PROXMIRE,
Chairman, Small Business Subcommittee, Committee on Banking and Currency,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: The National Association of Small Business Investment Companies is grateful to you for giving it this opportunity to comment upon the language of a proposed amendment to the Small Business Investment Act of 1958 covering the subject of self-dealing. Incidentally, as you know, I had not had an opportunity to see the amendment before I testified.

A literal reading of subsection (a) of the proposed amendment would make it appear that a licensee would be obliged to obtain prior Small Business Administration approval even where it was merely making an additional loan to or investment in a small business concern where the only affiliation arose out of a prior loan to or investment in the small business concern, or service by a principal of the licensee as a director of the small business concern, a common occurrence.

For example, where a licensee all of whose stock was held by one individual and which licensee had a 10 percent equity interest in the small business concern, the owner of the stock of the licensee might then be regarded as owning indirectly the stock of the small business concern acquired by the licensee. We assume that this result is not intended and thus would suggest the addition of language along the lines of rule 17a-6 promulgated by the Securities and Exchange Commission to exempt from certain provisions of section 17(a) of the Investment Company Act of 1940 those transactions where licensees are merely supplying additional funds to a portfolio company, or where one of its principals serves as a director of the borrowing concern.

The foregoing might be accomplished by relettering subsection (b) as subsection (c) and by inserting a new subsection (b) to read as follows:

"(b) This section shall not apply where the affiliations enumerated in subsection (a) hereof arise solely because of an affiliation created through (i) the owning, holding, or controlling with power to vote, directly or indirectly, by the licensee of the voting securities of such small business concern, (ii) the right of the licensee to nominate a director of such small business concern."

Subsection (b) of your draft appears to be unobjectionable, but subsection (c) raises several questions:

1. Is the borrower to be identified? The language asks only for the terms of the transaction and the nature of the affiliation.

2. What is the meaning of the phrase "the terms upon which the purchase or loan is to be made"? I would assume that this would require only the amount of the financing, the interest rate, the maturity, and the form of financing instrument utilized (note, convertible debenture, debenture with warrants, common stock, etc.). This should be carefully worded, since a loan agreement may run to 20 or 30 pages and it would be tragic if a Small Business Administration official interpreting the law were to rule that the entire agreement is encompassed in "terms of the loan."

3. In large cities, the cost of a legal notice is fairly substantial and might add appreciably to the cost of making a small loan or investment. Obviously, it would be unfortunate to establish this further factor against smaller loans or investments.

4. A more fundamental objection to this publication in the local press should also be made. I cannot see in what way the insertion of such a legal notice would serve to protect any of the various interests which might be involved. Could minority stockholders of either the borrower or the licensee be expected to read the legal notices daily? I very much doubt it. Furthermore, since the licensee would be required to publish the transaction only in a newspaper of general circulation "in the locality in which it has its principal place of business," such publication would not normally reach persons interested in the borrowing small business concern where it was located in some other city. But to require publication in newspapers of general circulation both in the licensee's headquarters city and in the hometown of the borrowing small business concern would only compound the expense problem.

5. Publication in the Federal Register of the bare essentials of the transaction appears reasonable—if the Congress decides that disclosure of the names of the borrowers is imperative. SEC follows the procedure of publishing notices relating to affiliated transactions in the Federal Register but does not require additional publication in newspapers of general circulation. It seems to us that the SEC procedures relating to publication should suffice for licensees.

After weighing all the proposals, I favor the plan put forth by the Small Business Administration. Over the years, this same sort of procedure has been utilized with great success by the Internal Revenue Service. The Small Business Administration plan alone will guarantee that Congress and the industry will be able to judge the criteria on which the Small Business Administration makes its decisions on self-dealing transactions. If names are withheld, the Small Business Administration will be able to set out its reasoning in detail without hurting the small business involved.

We thank you for this opportunity to amplify our testimony given to your subcommittee last week.

Sincerely yours,

JAMES W. HOWARD, *President.*

(The following three alternative proposed amendments were furnished by the subcommittee staff at the direction of the subcommittee to SBA and SEC for their consideration in preparing their testimony for these hearings:)

I. CONFLICT OF INTEREST

SEC. —. No licensee shall purchase equity securities of, or make any loan to, any small business concern, if—

(1) an officer or director of such licensee, or a close relative of such officer or director, is an officer or director, or owns or controls (directly or indirectly) 10 percent or more of the stock, of such concern;

(2) any person, owning or controlling (directly or indirectly) 10 percent or more of the stock of such licensee, also owns or controls (directly or indirectly), or is a close relative of any person who owns or controls (directly or indirectly), 10 percent or more of the stock of such concern; or

(3) any person who is an officer or director of such concern or who owns or controls (directly or indirectly) 10 percent or more of the stock of such concern, within six months prior to the making of any such purchase or loan, served as an officer or director, or owned or controlled (directly or indirectly) 10 percent or more of the stock, of such licensee.

II. CONFLICT OF INTEREST

SEC. —. (a) Without the prior approval of the Administration, no licensee shall purchase equity securities of, or make any loan to, any small business concern, if—

(1) an officer or director of such licensee, or a close relative of such officer or director, is an officer or director, or owns or controls (directly or indirectly) 10 percent or more of the stock, of such concern;

(2) any person, owning or controlling (directly or indirectly) 10 percent or more of the stock of such licensee, also owns or controls (directly or indirectly) 10 percent or more of the stock of such licensee, also owns or controls (directly or indirectly), or is a close relative of any person who owns or controls (directly or indirectly), 10 percent or more of the stock of such concern; or

(3) any person who is an officer or director of such concern or who owns or controls (directly or indirectly) 10 percent or more of the stock of such concern, within six months prior to the making of any such purchase or loan, served as an officer or director, or owned or controlled (directly or indirectly) 10 percent or more of the stock, of such licensee.

(b) No purchase or loan by a licensee requiring approval under this section shall be approved by the Administration, unless it finds that (1) a majority of the board of directors of such licensee have no interest (directly or indirectly) in the small business concern affected by such purchase or loan, except as may be incidental to and consistent with the conscientious performance of their duties as members of the board of directors of such licensee, (2) such purchase or loan has received the affirmative approval of such majority, and (3) the terms upon which such purchase or loan are to be made are not less favorable to such licensee than those offered by it to other small business concerns. Full details

of any transaction approved by the Administration under this section shall be included in the annual report filed by the Administration, under section 10 of the Small Business Act, for the year in which such transaction occurred.

III. CONFLICT OF INTEREST

SEC. —. No licensee shall purchase equity securities of, or make any loan to, any small business concern, if—

(1) an officer or director of such licensee, or a close relative of such officer or director, is an officer or director, or owns or controls (directly or indirectly) 10 percent or more of the stock, of such concern ;

(2) any person, owning or controlling (directly or indirectly) 10 percent or more of the stock of such licensee, also owns or controls (directly or indirectly), or is a close relative of any person who owns or controls (directly or indirectly), 10 percent or more of the stock of such concern ;
or

(3) any person who is an officer or director of such concern or who owns or controls (directly or indirectly) 10 percent or more of the stock of such concern, within six months prior to the making of any such purchase or loan, served as an officer or director, or owned or controlled (directly or indirectly) 10 percent or more of the stock, of such licensee ;

unless, within — days after the making of such purchase or loan, such licensee (A) gives notice thereof in writing to the Administration setting forth (i) the nature of the interest or interests requiring the giving of such notice, (ii) the vote by which its board of directors approved the transactions, (iii) the reasons why the purchase or loan was considered to be a sound investment, and (iv) the terms upon which the purchase or loan was made, and (B) causes to be published in a newspaper of general circulation in the locality in which it has its principal place of business a notice setting forth (i) the nature of the interest or interests requiring the giving of such notice, and (ii) the terms upon which the purchase or loan was made.

Senator PROXMIRE. The subcommittee will adjourn subject to the call of the Chair.

(Whereupon, at 1:15 p.m., the subcommittee was adjourned.)





