

Y4
B22/3
Sm 1/11/966

1035

894
B22/3
Sm 1/11/966
966

SMALL BUSINESS INVESTMENT ACT AMENDMENTS OF 1966

GOVERNMENT

Storage

HEARINGS BEFORE A SUBCOMMITTEE OF THE COMMITTEE ON BANKING AND CURRENCY UNITED STATES SENATE

EIGHTY-NINTH CONGRESS
SECOND SESSION

ON

S. 3695

A BILL TO AMEND THE SMALL BUSINESS INVESTMENT ACT
OF 1958, AND FOR OTHER PURPOSES

AUGUST 24 AND 25, 1966

Printed for the use of the
Committee on Banking and Currency

KSU LIBRARIES
111900 498154
✓



201/11
Baker
Baker
Baker

COMMITTEE ON BANKING AND CURRENCY

A. WILLIS ROBERTSON, Virginia, *Chairman*

| | |
|---------------------------------------|--------------------------------|
| JOHN SPARKMAN, Alabama | WALLACE F. BENNETT, Utah |
| PAUL H. DOUGLAS, Illinois | JOHN G. TOWER, Texas |
| WILLIAM PROXMIRE, Wisconsin | STROM THURMOND, South Carolina |
| HARRISON A. WILLIAMS, Jr., New Jersey | BOURKE B. HICKENLOOPER, Iowa |
| EDMUND S. MUSKIE, Maine | |
| EDWARD V. LONG, Missouri | |
| MAURINE B. NEUBERGER, Oregon | |
| THOMAS J. McINTYRE, New Hampshire | |
| WALTER F. MONDALE, Minnesota | |

MATTHEW HALE, *Chief of Staff*

WOODLIEF THOMAS, *Chief Economist*

JOHN R. EVANS, *Minority Chief of Staff*

HENRIETTA S. CHASE, *Chief Clerk*

SUBCOMMITTEE ON SMALL BUSINESS

WILLIAM PROXMIRE, Wisconsin, *Chairman*

| | |
|-----------------------------------|--------------------------------|
| A. WILLIS ROBERTSON, Virginia | JOHN G. TOWER, Texas |
| JOHN SPARKMAN, Alabama | STROM THURMOND, South Carolina |
| PAUL H. DOUGLAS, Illinois | BOURKE B. HICKENLOOPER, Iowa |
| MAURINE B. NEUBERGER, Oregon | |
| THOMAS J. McINTYRE, New Hampshire | |
| WALTER F. MONDALE, Minnesota | |

CONTENTS

| | |
|--------------|-----------|
| S. 3695..... | Page 2 |
|--------------|-----------|

WITNESSES

WEDNESDAY, AUGUST 24

| | |
|--|----|
| Bernard L. Boutin, Administrator, Small Business Administration..... | 13 |
| Grogan Lord, president, National Association of Small Business Investment Companies; accompanied by Walter B. Stults, executive director, and Charles M. Noone, general counsel..... | 1 |
| Don A. Christensen, president; and Mark Rollinson, vice president and house counsel, Greater Washington Industrial Investments, Inc..... | 43 |

THURSDAY, AUGUST 25

| | |
|--|----|
| Fred R. Harris, a U.S. Senator from the State of Oklahoma..... | 53 |
|--|----|

ALPHABETICAL LIST OF WITNESSES

| | |
|---|----|
| Boutin, Bernard L., Administrator, Small Business Administration..... | 13 |
| Christensen, Don A., president, Greater Washington Industrial Investments, Inc..... | 43 |
| Harris, Fred R., U.S. Senator from the State of Oklahoma..... | 53 |
| Lord, Grogan, president, National Association of Small Business Investment Companies..... | 31 |
| Rollinson, Mark, vice president and house counsel, Greater Washington Industrial Investments, Inc..... | 46 |
| Stults, Walter B., executive director, National Association of Small Business Investment Companies..... | 40 |

STATEMENTS AND DATA

| | |
|--|----|
| Comments on S. 3695 by Greater Washington Industrial Investments, Inc.. | 43 |
| Copy of proposed bill of Senator Fred R. Harris..... | 54 |
| Harris, Fred R., U.S. Senator from the State of Oklahoma: Prepared statement..... | 64 |
| Memorandum, to Jerome S. Alderman, from John Brick, re proposed legislation on small business investment companies..... | 57 |
| Proposed revision of section 5 of S. 3695..... | 12 |
| Revised version of S. 3695 as prepared by the staff..... | 75 |
| Side-by-side comparison of proposed SBIC legislation..... | 58 |
| Statement of Fred R. Harris, a U.S. Senator from Oklahoma, at Permanent Investigations Subcommittee hearings..... | 61 |
| Summary of bill to strengthen certain provisions of law relating to the organization, operation, and supervision of small business investment companies..... | 60 |
| United States Code, title 18, excerpts from..... | 66 |

REVIEWS

REVIEWS

REVIEWS

The first part of the book is devoted to a general introduction to the subject of the book. The author discusses the importance of the subject and the scope of the book. He also discusses the organization of the book and the methods used in the research.

REVIEWS

The second part of the book is devoted to a detailed discussion of the subject. The author discusses the various aspects of the subject and the methods used in the research.

REVIEWS

The third part of the book is devoted to a detailed discussion of the subject. The author discusses the various aspects of the subject and the methods used in the research.

REVIEWS

The fourth part of the book is devoted to a detailed discussion of the subject. The author discusses the various aspects of the subject and the methods used in the research.

SMALL BUSINESS INVESTMENT ACT AMENDMENTS OF 1966

WEDNESDAY, AUGUST 24, 1966

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

The subcommittee met at 10:15 a.m. in room 5302, New Senate Office Building, Senator William Proxmire, chairman of the subcommittee, presiding.

Present: Senators William Proxmire, John Sparkman, John G. Tower, and Strom Thurmond.

Senator PROXMIRE. Today the Senate Small Business Subcommittee is holding hearings on S. 3695, a bill to amend the Small Business Act, and for other purposes.

S. 3695 was introduced by myself, and Senators Sparkman, Harris, Tower, and Mundt. It is recommended by the Small Business Administration.

This bill would provide additional tools to the Administrator of the SBA to supervise the small business investment company program. It would also provide administrative changes in the organization of the SBA. Recent hearings by this subcommittee, the Senate Permanent Subcommittee on Investigations under the chairmanship of Senator Harris of Oklahoma, and the House Select Committee on Small Business have shown that there have been many violations of the Small Business Investment Act and regulations. The amendments contained in this bill would enable the SBA to move more effectively and with more speed in removing wrongdoers from the SBIC program by improving the present administrative and legal proceedings.

(The bill and the proposed revision of section 5 follows:)

89TH CONGRESS
2^D SESSION

S. 3695

IN THE SENATE OF THE UNITED STATES

AUGUST 8, 1966

Mr. PROXMIRE (for himself, Mr. SPARKMAN, Mr. HARRIS, Mr. TOWER, and Mr. MUNDT) 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, and for other purposes.

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 1966".

5 SEC. 2. (a) Title II of the Small Business Investment
6 Act of 1958 is repealed.

7 (b) The table of contents of such Act is amended—

8 (1) by striking out that part which describes the
9 contents of title II;

10 (2) by inserting at the end of that part which de-
11 scribes the contents of title III the following new items:

"Sec. 313. Unlawful acts and omissions by officers, directors, employees or agents; breach of fiduciary duty.

"Sec. 314. Penalties and forfeitures.

"Sec. 315. Civil liability of officers and directors.

"Sec. 316. Jurisdiction and service of process."; and

1 (3) by striking out the items describing the con-
2 tents of sections 309 and 310 and inserting in lieu
3 thereof the following:

"Sec. 309. Revocation and suspension of licenses; cease and desist orders.

"Sec. 310. Examinations and investigations."

4 SEC. 3. Section 308 of the Small Business Investment
5 Act of 1958 is amended—

6 (1) by striking out the last two sentences of sub-
7 section (c); and

8 (2) by inserting after subsection (e) the follow-
9 ing new subsection:

10 “(f) In the performance of, and with respect to the
11 functions, powers, and duties vested by this Act, the Admin-
12 istrator and the Administration shall (in addition to any
13 authority otherwise vested by this Act) have the functions,
14 powers, and duties set forth in the Small Business Act, and
15 the provisions of sections 13 and 16 of that Act, insofar as
16 applicable, are extended to the functions of the Administrator
17 and the Administration under this Act.”

18 SEC. 4. Section 310 of the Small Business Investment
19 Act of 1958 is amended—

20 (1) by striking out the section heading and in-

1 serting in lieu thereof "Examinations and Investiga-
2 tions"; and

3 (2) by inserting "(a)" after "SEC. 310.", and
4 by adding at the end thereof a new subsection as
5 follows:

6 "(b) (1) Each small business investment company
7 shall be subject to examinations made by direction of the
8 Administration by examiners selected or approved by the
9 Administration, and the cost of such examinations, including
10 the compensation of the examiners, may in the discretion of
11 the Administration be assessed against the company exam-
12 ined and when so assessed shall be paid by such company.
13 Every such company shall make such reports to the Admin-
14 istration at such times and in such form as the Administra-
15 tion may require; except that the Administration is author-
16 ized to exempt from making such reports any such company
17 which is registered under the Investment Company Act of
18 1940 to the extent necessary to avoid duplication in report-
19 ing requirements.

20 "(2) Each small business concern which has received
21 financial assistance from a small business investment com-
22 pany pursuant to this Act shall, when in the opinion of the
23 Administrator it is necessary and appropriate, be subject to
24 examinations made by direction of the Administration by

1 examiners selected or approved by the Administration. The
2 cost of such examinations shall be paid from the business
3 loan and investment fund established by section 4 (c) of
4 the Small Business Act.”

5 SEC. 5. (a) Section 309 of the Small Business Invest-
6 ment Act of 1958 is amended by striking out the section
7 heading and inserting in lieu thereof the following:

8 “REVOCATION AND SUSPENSION OF LICENSES; CEASE AND
9 DESIST ORDERS”

10 (b) Section 309 (a) of such Act is amended—

11 (1) by inserting “revoked or” before “suspended”;

12 (2) by striking out in paragraph (1) “Adminis-
13 tration, for the purpose of obtaining the license” and in-
14 serting in lieu thereof “Administration”; and

15 (3) by striking out in paragraph (2) “for the pur-
16 pose of obtaining the license,”.

17 (c) Section 309 (b) of such Act is amended to read as
18 follows:

19 “(b) Where a licensee or any other person has not
20 complied with any provision of this Act, or of any regula-
21 tion issued under this Act by the Administration, or is
22 engaging or is about to engage in any acts or practices
23 which constitute or will constitute a violation of such Act
24 or regulation, the Administration may order such licensee
25 or other person to cease and desist from such action or fail-

1 ure to act. The Administration may further order such
2 licensee or other person to take such action or to refrain
3 from such action as the Administration deems necessary to
4 insure compliance with the Act and the regulations. Such
5 orders may, wherever appropriate as a result of violation of
6 section 313 hereof, direct the removal of any officer, di-
7 rector, employee, or agent of a licensee, and prohibit fur-
8 ther participation, directly or indirectly, in the conduct of
9 the affairs or management of the licensee on the part of
10 any person in violation of section 313. The Administration
11 may also suspend the license of a licensee, against whom an
12 order has been issued, until such licensee complies with
13 such order.”

14 (d) Section 309 (c) of such Act is amended—

15 (1) by inserting after “licensee”, each place it
16 appears, the following: “or other person”; and

17 (2) by inserting before “suspending”, each place
18 it appears, the following: “revoking or”.

19 (e) Section 309 (e) of such Act is amended by in-
20 serting after “licensee”, the first place it appears, the fol-
21 lowing: “or other person against whom an order is issued”.

22 (f) Section 309 (f) of such Act is amended—

23 (1) by striking out the first sentence and inserting
24 in lieu thereof the following: “If any licensee or other

1 person against which or against whom an order is
2 issued under this section fails to obey the order, the
3 Administration may apply to the United States court
4 of appeals, within the circuit where the licensee has its
5 principal place of business, for the enforcement of the
6 order, and shall file a transcript of the record upon
7 which the order complained of was entered.”; and

8 (2) by inserting “or other person” before the
9 period at the end of the second sentence.

10 SEC. 6. The Small Business Investment Act of 1958 is
11 further amended by adding at the end thereof the following
12 new sections:

13 “UNLAWFUL ACTS AND OMISSIONS BY OFFICERS, DIREC-
14 TORS, EMPLOYEES, OR AGENTS; BREACH OF FIDUCIARY
15 DUTY

16 “SEC. 313. (a) Wherever a licensee violates any pro-
17 vision of this Act or regulation issued thereunder by reason
18 of its failure to comply with the terms thereof or by reason
19 of its engaging in any act or practice which constitutes or
20 will constitute a violation thereof, such violation shall be
21 deemed to be also a violation and an unlawful act on the
22 part of any person, including the individual officers, direc-
23 tors, or employees or agents of such licensee who, directly
24 or indirectly, authorizes, orders, participates in, or causes,
25 brings about, counsels, aids or abets in the commission of

1 any acts, practices or transactions which constitute or will
2 constitute, in whole or in part, such violation.

3 “(b) It shall be unlawful for an officer, director, em-
4 ployee, agent or other participant in the management or
5 conduct of the affairs of the licensee to engage in any act or
6 practice, or to omit any act, in breach of his fiduciary duty
7 as such officer, director, employee, agent or participant in
8 the management or conduct of the affairs of the licensee if,
9 as a result thereof, the licensee has suffered or is in imminent
10 danger of suffering financial loss or other damage.

11 “(c) Except with the written consent of the Admin-
12 istration, it shall be unlawful (1) for any person to here-
13 after take office as an officer, director, employee, agent or
14 participant in the conduct of the affairs or management of
15 a licensee who has been convicted of any felony or any
16 criminal offense involving dishonesty or a breach of trust,
17 or who has been found civilly liable in damages, or has been
18 permanently or temporarily enjoined by an order, judgment
19 or decree of any court of competent jurisdiction, by reason
20 of any act or practice involving fraud or breach of trust; or
21 (2) for any person to continue to serve in any of the above
22 capacities described in this subsection who is hereafter con-
23 victed of any felony or criminal offense involving dishonesty
24 or breach of trust, or who is hereafter found civilly liable
25 in damages, or permanently or temporarily enjoined by an

1 order, judgment or decree of any court of competent juris-
2 diction, by reason of any act or practice involving fraud or
3 breach of trust.

4 "PENALTIES AND FORFEITURES

5 "SEC. 314. A licensee which violates any regulation,
6 or written directive issued by the Administrator, requiring
7 the filing of any regular or special report pursuant to section
8 310 (b) of this Act, shall forfeit and pay to the United
9 States a civil penalty of not more than \$100 for each and
10 every day of the continuance of the licensee's failure to file
11 such report. The civil penalties provided for in this section
12 shall accrue to the United States and may be recovered by
13 the United States in a civil action brought by the United
14 States.

15 "CIVIL LIABILITY OF OFFICERS AND DIRECTORS

16 "SEC. 315. Any officer or director of a licensee who
17 knowingly participates, directly or indirectly, in a violation
18 of this Act or regulation or orders thereunder relating to the
19 disbursement of funds or lending of credit by such licensee,
20 shall be personally liable for, and shall unconditionally guar-
21 antee repayment to the Administration, of all indebtedness
22 then owing to the Administration by the licensee, and shall
23 be personally liable for all such indebtedness as and when
24 it becomes due and payable, whether by acceleration or
25 otherwise, as well as court costs and reasonable attorneys'

1 fees incurred in collecting such indebtedness: *Provided,*
2 *however,* That no such guarantee or personal liability shall
3 exceed the lesser of the amount of loss or damage incurred
4 by the licensee as a consequence of such violation, or the
5 amount of the indebtedness then owing to the Administration
6 by the licensee. No other action of any nature under this
7 Act shall affect the liability of any officer or director im-
8 posed by this section for acts or omissions to act.

9 "JURISDICTION AND SERVICE OF PROCESS

10 "SEC. 316. Any suit or action brought under sections
11 308, 311, 314, or 315 by the Administration at law or in
12 equity to enforce any liability or duty created by, or to en-
13 join any violation of this Act or rules or regulations or orders
14 promulgated thereunder, shall be brought in the district
15 wherein the licensee maintains its principal office, and pro-
16 cess in such cases may be served in any district in which
17 the defendant maintains its principal office, or transacts busi-
18 ness, or wherever the defendant may be found."

19 SEC. 7. Section 311 of the Small Business Investment
20 Act of 1958 is amended by adding at the end thereof the
21 following new subsection:

22 "(c) The Administration shall have authority to act
23 as trustee or receiver of the licensee. Upon request by the
24 Administration, the court may appoint the Administration
25 to act in said capacity unless the court deems such appoint-

1 ment inequitable or otherwise inappropriate by reason of the
2 special circumstances involved.”

3 SEC. 8. (a) Section 4 (b) of the Small Business Act
4 is amended by striking out “three Deputy Administrators”
5 and inserting in lieu thereof “a Deputy Administrator and
6 three Associate Administrators”.

7 (b) Such section is further amended by adding at the
8 end thereof the following: “The Deputy Administrator shall
9 be Acting Administrator of the Administration during the
10 absence or disability of the Administrator or in the event
11 of a vacancy in the office of the Administrator”.

PROPOSED REVISION OF SECTION 5 OF S. 3695

SEC. 5. (a) Section 309 of the Small Business Investment Act of 1958 is amended by striking out the section heading and inserting in lieu thereof the following: "REVOCATION AND SUSPENSION OF LICENSES; REMOVAL OF OFFICIALS; CEASE AND DESIST ORDERS".

(b) Section 309 (a) of such Act is amended to read as follows:

"Sec. 309. (a) A license may be revoked or suspended by the Administration—

"(1) for false statements knowingly made in any written statement required under this title, or any regulation issued pursuant thereto;

"(2) for knowingly failing to state a material fact necessary in order to make any written statement, required under this title, or any regulation issued pursuant thereto, not misleading in the light of the circumstances under which such statement was made;

"(3) for willful or repeated violation of, or willful or repeated failure to observe, any provision of this Act;

"(4) for willful or repeated violation of, or willful or repeated failure to observe, any rule or regulation of the Administration authorized by this Act; or

"(5) for violation of, or failure to observe, any cease and desist order issued by the Administration under this section.

The Administration may, in connection with, or in lieu of, revoking or suspending the license of any licensee under this subsection, order the removal of any officer, director, employee, or agent of such licensee, if it determines that such officer, director, employee, or agent knowingly authorized, ordered, or participated in any act or practice referred to in clauses (1) to (5) above."

(c) Section 309 (b) of such Act is amended to read as follows:

"(b) Where a licensee or any other person has failed to comply with any provision of this Act, or of any regulation issued pursuant thereto, or is engaging, or is about to engage (as determined by the Administration upon reasonable cause), in any acts or practices which constitute or will constitute a violation of such Act or regulation, the Administration may order such licensee or other person to cease and desist from such acts or practices or from such failure to comply, as the case may be. The Administration may further order such licensee or other person to take such action or to refrain from such action as the Administration deems necessary to insure compliance with this Act and the regulations issued pursuant thereto. The Administration may also suspend the license of a licensee against whom an order under this subsection has been issued, until such licensee complies with such order."

(d) Section 309 (c) of such Act is amended to read as follows:

"(c) Before revoking or suspending a license, or removing an officer, director, employee, or agent pursuant to subsection (a), or issuing a cease and desist order pursuant to subsection (b), the Administration shall serve upon the licensee or other person involved an order to show cause why an order revoking or suspending the license, or an order removing an officer, director, employee, or agent, or an order to cease and desist should not be issued. Any such order to show cause shall contain a statement of the matters of fact and law asserted by the Administration and the legal authority and jurisdiction under which a hearing is to be held, and shall inform the licensee or other person that a hearing will be held before the Administration at a time and place stated in the order. If after hearing, or a waiver thereof, the Administration determines on the record that an order revoking or suspending the license, or an order removing an officer, director, employee, or agent, or an order to cease and desist should issue, it shall promptly issue such order, which shall include a statement of the findings of the Administration and the grounds and reasons therefor and specify the effective date of the order, and shall cause the order to be served on the licensee or other person."

(e) Section 309 (e) of such Act is amended by inserting after "licensee", in the first sentence the following: "or other person against whom an order is issued".

(f) Section 309 (f) is amended—

(1) by striking out the first sentence and inserting in lieu thereof the following:

"If any licensee or other person against which or against whom an order is issued under this section fails to obey the order, the Administration may apply to the United States court of appeals, within the circuit where the licensee has

its principal place of business, for the enforcement of the order, and shall file a transcript of the record upon which the order complained of was entered.”; and (2) by inserting “or other person” before the period at the end of the second sentence.

Senator PROXMIRE. During the next session I plan to introduce and push for legislation to provide additional incentives for the SBIC program. Additional leverage and tax benefits are badly needed. I will do all that I can to see that they are provided. I have talked with other members of the committee, Senator Sparkman and others, and there is a strong and general feeling that such additional legislation is needed. Indeed, Senator Sparkman introduced legislation of this kind in the past and we will do all we can to get action on it.

When the Small Business Investment Act was passed in 1958, some tax incentives were included in a companion bill. Experience has shown that these incentives are not enough. In order to provide additional tax incentives for SBIC's, Senator Sparkman introduced S. 1854 last year. Similar bills were also introduced in the 87th and 88th Congresses. No position has been taken by the Treasury Department on S. 1854. I have encouraged the Treasury Department and the SBA to work together to see if some agreement can be reached on the provisions of this tax bill.

It is my understanding these conversations are underway now and I hope they will come to fruition shortly on a bill we can move and support.

We must also develop an acceptable method of providing more leverage to SBIC's. Senator Sparkman and I have sponsored in this Congress S. 1888, the Sparkman bill, a bill which would provide for a small business capital bank. The administration has not taken a position on this bill. We must take a new look at this leverage problem and come up with a solution which will benefit SBIC's in this important area.

I would like to repeat now what I have said several times in the past: I am convinced that the SBIC program is a good program. It is serving a vitally needed role in the financing of small businesses. We must find ways to keep efficient people in the program and to attract competent new people in the program and to make sure we get the kind of capital we must have if this program will work. This must be done, and I believe we can do it.

Our first witness today is the Honorable Bernard L. Boutin, Administrator of the Small Business Administration.

STATEMENT OF BERNARD L. BOUTIN, ADMINISTRATOR, SMALL BUSINESS ADMINISTRATION, WASHINGTON, D.C.

Mr. BOUTIN. Thank you very much Mr. Chairman and members of the committee.

The purpose of this hearing is to consider the bill which you have introduced (S. 3695) to improve the organization of the Small Business Administration and to strengthen the regulatory powers of the agency over the small business investment company program established by the Small Business Investment Act of 1958. I welcome the opportunity to present my views on this important measure.

The SBIC program is an imaginative approach to solving the long-term credit and equity financing problems encountered by many small

firms. It combines Government funds with the talent and capital of private industry. I believe this is a creative partnership and should be both preserved and strengthened.

Nevertheless the industry has, as you know, encountered problems. Not the least of these problems are those which arise from violations of the act and our regulations by some small business investment companies. I will not dwell upon the need for tightened enforcement, because that need has already been demonstrated in hearings held by this subcommittee and by other committees of the Congress.

Your bill will provide SBA with the tools needed for tighter enforcement. I would like to review with you and your colleagues the key features of S. 3695.

Section 2 of the bill repeals title II of the Small Business Investment Act of 1958, which I will refer to hereafter in this statement as the "act."

In contrast to the other divisions of the Small Business Administration, which are creatures of the Administrator and can be abolished or reformed by him at any time, the Investment Division—ID—is established by title II on a statutory basis. In substance, title II also provides that the powers conferred upon the administration under the act are to be exercised by the administration through the Investment Division and that the powers conferred upon the Administrator thereunder are to be exercised by him through the Deputy Administrator in charge of such division.

Title II could be, perhaps has been, construed as meaning that all actions by the Administrator pursuant to the act must, without exception, be taken by him through the Deputy Administrator for ID. Such an interpretation is erroneous, because it is entirely inconsistent with the responsibilities vested in the Administrator by the act. Rather, the underlying intent to title II is simply that ID is to be the normal instrumentality of the Administrator in promoting the small business investment program. It does not preclude him from taking direct action, independently of ID, where he finds such action appropriate.

The repeal of title II, placing ID on the same basis as the other division of SBA, will eliminate any question as to the validity of actions taken by the Administrator. Such clarification is particularly important at the present time in view of the extensive efforts which I am now making to strengthen the small business investment company program.

The repeal of title II should be viewed as a prelude to a more successful, a more effective program. It opens the way to more extensive supervision and more active participation by the Administrator. It brings to the investment program all of the benefits of a diversified agency with wide experience in conducting financial and management assistance programs.

A related organization change, contemplated by section 8 of the bill, revises the title of the present Deputy Administrators to that of Associate Administrators. At the same time it authorizes the appointment of a single Deputy Administrator to assist the Administrator. This new Deputy will be empowered to function as Acting Administrator during the absence or disability of the Administrator or in the event of a vacancy in the Office of Administrator.

At the present time SBA is one of the few agencies of the Government which lacks specific authorization for such an acting head. This should be remedied.

It is important to note that the salaries and status of the present Deputy Administrators are not affected by the proposed change. Under perfecting language which we are submitting, the Deputy Administrator would be established at level IV of the pay scale and the Associate Administrators, the present Deputy Administrators, would remain at level V.

Section 7 of the bill would authorize SBA to act as trustee or receiver of an SBIC, when so appointed by a court. This proposal is in the nature of a clarifying amendment. It is believed that the authority already exists. In at least one case, it has been exercised.

Experience has demonstrated the difficulty of obtaining a qualified person to act as trustee or receiver of an SBIC. In many cases the search for such a person has led to delays during which the position of the company has deteriorated. In other cases unqualified appointees, finding themselves unable to handle the affairs of the company, have asked the court to be relieved.

In large part this situation is due to the fact that SBIC's represent a relatively new type of financial institution whose nature and characteristics are not commonly known, even among people otherwise versed in the fields of banking and investment. Similarly, the applicable laws and regulations are not widely known and understood.

On the other hand, SBA has at its disposal personnel who are familiar with the industry and who, in most cases, are familiar also with the background of the particular SBIC involved—its problems and the causes thereof, the nature of its investments, its financial status, and so forth. Such knowledge, which cannot readily be transmitted to a person new to the situation, may thus be promptly brought into play by the appointment of SBA as trustee or receiver.

In every instance, it should be noted, the question whether SBA is to be appointed as trustee or receiver rests entirely with the court. Such an appointment would never be made where it would be to the disadvantage of creditors of the SBIC other than SBA. The agency would serve only where it is the principal creditor or, as is often the case, the sole creditor.

In substance, section 5 of the bill would authorize SBA to revoke by administrative action the licenses of SBIC's guilty of violation so serious as to call for their removal from the program. The only existing means of obtaining this result is through court action, pursuant to section 308(d) of the act, entailing the delays which usually accompany such litigation.

Specifically, such administrative revocation would be authorized for willful or repeated failure to observe any provision of the act or any rule or regulation issued thereunder; or for willful or persistent violation of any cease and desist order issued by SBA. It would also be authorized for falsehoods or misleading assertions knowingly included in any statement section or any statement required by SBA.

Under existing law, the strongest administrative sanction available for such offenses is suspension of the violator's license; and, in the case of falsehoods or misleading assertions, even this remedy can be invoked only where the statement involved was filed for the purpose of obtaining a license.

Suspension is not an adequate administrative tool for dealing with SBIC's which have demonstrated, by the gravity of their offenses, that they are beyond redemption. In such cases suspension does not reach the issue, because it contemplates the eventual restoration to the program of parties who probably should not remain in it.

Typically, the more appropriate solution is prompt revocation, prompt expulsion from the program. Section 5 of the bill would provide this solution without depriving such companies of their rights. It should be emphasized that they would enjoy all of the protection afforded by the Administrative Procedure Act, and by judicial review, against arbitrary action.

This administrative authority will be particularly useful as a means of removing from the program inactive SBIC's—the ones which have simply sat on their funds, including those obtained from the Government, and refused to use them for the benefit of small business.

In substance, section 6 of the bill provides that a violation of the act or the regulations by an SBIC is, at the same time, a violation on the part of the officers, directors, or agents of the company who participated in or were otherwise responsible for the company's violation. This is a recognition of the fact that a company can act only through its management personnel and that the guilt for the company's violation is basically theirs.

At the present time SBA can proceed only against the SBIC. Such a proceeding, not including as parties the people who actually committed the offense, can hardly produce satisfactory results. Moreover, it is an anomaly to authorize SBA to investigate individuals as well as SBIC's, pursuant to section 310 of the act, and at the same time deny the agency a prompt and effective means of following up on resulting evidence of violations by such individuals.

The amendment, permitting us to reach beyond the company and deal directly with the offenders themselves, will greatly strengthen our enforcement. We would order them, as individuals, to take such action or refrain from such action as may be necessary to remedy the situation. Since failure to comply would expose them to personal liability, such orders will be much more effective than those issued against a company.

In further contrast to existing law, section 5, authorizes SBA to prohibit by administrative action violations which, though not yet consummated, are about to be committed. For example, SBA may discover, while it is still in the executory state, a contract made by an SBIC calling for the performance of an action which will violate the law or the regulations. The agency should not be compelled to wait until the performance occurs. Nor should it be limited to court action, pursuant to section 311 of the act, as a means of preventing it. Since time may be of the essence in such a case, SBA should have at its disposal the prompt administrative remedy proposed by section 5.

A related feature of the bill, also contained in section 5, is authority for SBA to direct by administrative action the removal of an SBIC official who violates the act or the regulations and to prohibit him from further participation in the conduct of the company—subject, of course, to the safeguards of the administrative procedure act. Such action would be taken only where serious offenses are involved and only where there is no other means of insuring against a repetition of them.

The removal authority we are requesting is, essentially, a means of saving SBIC's which might otherwise be lost to the program. It will be useful in cases where one or more individuals associated with a company, rather than the company itself, are the root of the trouble.

As a means of minimizing the number of potential troublemakers in the program, section 6 of the bill prohibits any one from hereafter becoming an SBIC official, without the written consent of the Administrator, who has been convicted of felony or of any crime involving dishonesty or breach of trust or who had had a judgment or court order entered against him in civil proceedings for conduct involving dishonesty or breach of trust. Similarly a person already serving as an SBIC official will not be permitted to continue if he hereafter commits such an offense.

This in my mind makes much sense.

Section 6 of the bill contains a provision that any officer or director of an SBIC who knowingly participates in a violation of the act or the regulations relating to the disbursement of funds or the lending of credit by the company shall be personally liable for, and shall unconditionally guarantee repayment to SBA, of all indebtedness then owing to SBA by the company, in no case, however, shall such guarantee or personal liability exceed the lesser of the amount of the resulting loss or damage incurred by the company or the amount of the indebtedness then owing to SBA by the company.

This feature of the bill is directed against individuals who convert to their own use the funds of a company, including the funds furnished by the Government, and thus reduce it to an empty shell. Under existing law our only remedy is against the shell. This amendment would make the guilty parties personally accountable.

It is hardly necessary to say that this new liability has no practical significance for the great majority of the people in the industry. The honest have nothing to fear from it. The target is the unscrupulous elements in the program which, though small enough, presents a real problem.

We must be tough with wrongdoers. This proposal is a measure of my determination to have a full reckoning with anyone who hereafter diverts to his pockets the funds this Government is putting into the program for the benefit of small business.

Another judicial sanction we are requesting is the establishment of penalties and forfeitures for SBIC's which fail to make timely filings of reports required by the act or the regulations. There is going to be no more coaxing or hesitation in dealing with delinquents. The bill would authorize a penalty of up to \$100 per day for every day of delay. Finally, the bill closes a jurisdictional loophole which has sometimes prevented us from taking action in a single court proceeding against both an SBIC and its officials.

Section 4 of the bill would authorize SBA to examine small firms receiving financial assistance from SBIC's, where the administrator considers such examination necessary or appropriate.

There are a number of reasons why SBA may have reason to conduct such an examination, and they all spring from our duty to insure that SBIC's are operating in accordance with the provisions of the act and our regulations. To take an outstanding example, we cannot always tell by examining the books of an SBIC whether its capital

has become impaired. Where we have reason to suspect that one or more of its larger investments is unsound, thereby creating danger of impairment, there is only one sure way to get the answer: we have to look at the condition of the recipients of those investments.

We sometimes have difficulty in obtaining such a look, because we lack clear authority to examine portfolio companies. Small firms may be reluctant to submit. We believe that the proposed amendment, providing us with clear authority, would make small firms more receptive to examination by us. It would thus facilitate our efforts to insure that SBIC's are operating in accordance with the provisions of the act and the regulations.

Let me emphasize that there would be no stigma attached to the small business in being examined by SBA. Indeed, in some cases, as where the SBIC has overreached or misrepresented to the detriment of the small concern, the SBA examination could help the small firm by enabling corrective action. And it should be remembered that any such examination could be made only when considered necessary or appropriate in the opinion of the Administrator.

The examination procedure would allow SBA to readily verify the books of an SBIC against the books of a portfolio small concern. It also could be useful in situations where an SBIC is in liquidation, or has been liquidated and SBA, as creditor, has had to take over its portfolio.

By providing a means for checking portfolio small concerns in connection with the examination of SBIC's, this amendment would greatly improve the efficiency and effectiveness of SBA's regulatory operations.

Mr. Chairman, we believe that this legislation is urgently needed. The SBIC program, once it is operating properly, has enormous potential. The sooner we can make sure that it does operate properly, the sooner this potential will be realized.

I would like to say for the information of the committee, Mr. Chairman, that I have a letter now from the Bureau of the Budget. As we promised, we discussed with them the proposed legislation and I have a letter from the Bureau dated August 23, the significant part of the letter stating "you are advised that enactment of H.R. 16934 and Senate bill 3695 would be consistent with the administrations objectives."

Thank you.

Senator PROXMIRE. As you may have anticipated, Mr. Boutin, there are some provisions in this bill that are highly controversial, certainly within the SBIC industry among the people who have contributed very greatly, I am sure in your judgment and my judgment, to the success of this program. If it is going to really succeed in the future, I think that their cooperation and their goodwill is very, very important.

I would like to raise some of these questions, I am sure other members of the committee are concerned with the same questions and I would invite other members of the committee at any time—I will try to keep my interrogation brief but because I will cover various areas, if they want to come in and question the intent on any issue I am questioning on they are welcome.

I know their time is valuable and they may have to leave for other business because we are in the hope of closing—

Mr. BOUTIN. If I could interrupt, Mr. Chairman, we haven't had our appropriation yet so don't leave yet, please. We need that.

Senator PROXMIRE. Well, you say in your statement here that the honest will have nothing to fear from this program. There seems to be a strong feeling on the part of some very honest and able people that they would have plenty to fear from this bill, they think, no matter how sincere and competent the administration was under it.

I would like to raise a particular question to begin with. I am referring to the provisions of section 6 which would impose a personal liability on any officer or director of an SBIC who knowingly participates in a violation of the act or regulation.

The first question is this: Don't you think this provision should be clarified in order to prevent the imposition of this liability based on a mistake in judgment on the part of the officer or director which resulted in the breach of the act or regulation?

I am thinking of the fact that we just passed a financial institutions bill which was only passed in my judgment because it provided that only where there was clear personal dishonesty on the part of the officer or director was he subject to removal. Here we don't have any provision of that kind in this bill.

Mr. BOUTIN. As the chairman well knows, from our continuous examination of the program, this bill represents, to our best judgment, the tools that we feel we badly need in order to have the proper type of regulation, for the program. I am obviously no expert in matters of law. I am not an attorney. My whole concept in developing this bill, and in talking to our people who put the nuts and bolts of the language together, was that we do not want tools made available by statute that can be administered capriciously or arbitrarily. We are concerned with the welfare of this program. We hope to have a legislative package ready to submit to the 90th Congress to provide new incentives and new tools to help the program succeed.

Today, however, we are talking about tools that the Administrator needs in order to do this job properly. Now, as I am sure the committee knows, there are precedents for personal liability. There are three, at least, that I have been able to find out about.

They are the Investment Company Act of 1940, the Securities Exchange Act, and the National Banking Act—which parallels very much what we are asking of the Congress, at this time.

Senator PROXMIRE. I wish, if you have a chance to do so, you would review those particular acts to see if they do parallel what you are asking, in terms of imposing a liability to this extent, even where there is no evidence of personal dishonesty.

Mr. BOUTIN. The one point, Mr. Chairman, that I would like to make is I would not like to see legislation passed which does not include personal liability at least in those cases where orders of cease and desist have been issued. Nevertheless, the individuals have gone merrily along their way and gone ahead and done it. It may not be a dishonest act, but certainly an act that was clearly contrary to instructions of the regulatory agency.

I think clearly that there ought to be personal liability in those cases.

Senator PROXMIRE. Let me give you some specific examples.

Supposing SBIC makes a loan which, in your opinion is not adequately secured, as required by the 1958 act. Would you hold the principals of the SBIC liable under this section?

Mr. BOUTIN. No; we would not. We would not, unless we had told them, because of knowledge that we had beforehand, that this was a poor loan, a loan that shouldn't be made, or it was a transaction that shouldn't be made, because it was contrary to our regulation.

Senator PROXMIRE. In other words, what you are saying is that you would have had to have warned against that particular investment before you would take action under this provision?

Mr. BOUTIN. That is correct. If we are simply talking now about a matter of judgment and not a violation of regulation—in other words, my concept of this, Mr. Chairman—

Senator PROXMIRE. It could be a violation of regulation. For instance, we had an example of what I thought was a fine contribution the SBIC's made to this company in Wausau, which is in Wisconsin, the Marathon Co., a bankrupt company. An SBIC came along and made a \$500,000 investment. Because of that investment, \$400,000 of bank money came in, in addition to that.

The company was saved. Now a profitable operation. Five hundred jobs saved. This was a bankrupt company.

It seems to me you can make a strong case that this may well have been a violation of regulation and of law.

Section 305(e) says any investment made under this section shall be of such sound value, as reasonably to assure repayment. So this loan to a bankrupt company could have been construed as such a violation.

Under those circumstances the SBIC, which I thought, and still think, was almost heroic in the contribution, would have been subject to a terrific liability.

Mr. BOUTIN. Of course, we can find all kinds of exceptions, as the chairman and members of the committee well know, but I think if we open the door to a relief of personal liability when there is an outright violation of law or regulation, we are doing the program a disservice.

Now, this particular company you spoke about, I am aware of that case. I am not aware of any possible violation of our regulations, but, if there were, or if there was a question of violation, the SBIC could have picked up the telephone, if they were willing to risk \$500,000 to loan this company, and discussed it with the Investment Division.

Senator TOWER. In connection with what my distinguished colleague from Wisconsin has asked, is it not true that although this may not be commonplace there are other instances where the SBIC has gone in and saved a company that was bankrupt or on the verge of bankruptcy?

Mr. BOUTIN. Oh, I think there are many instances of that Senator Tower, without any question at all.

Senator TOWER. I am wondering if this legislation isn't sufficiently severe that it would be something of an inhibition on the SBIC in their efforts to perhaps save some of these companies?

Mr. BOUTIN. Of course, this proposed legislation goes to really three points. The violation of the law, not just this law but existing law. The violation of SBA's regulation, and finally, acts of outright dishonesty, putting money in their own pockets, and so forth.

We are not looking for any statutory authority that would be overly restrictive, but, as we operate now our hands are pretty much tied, as I am sure the Senator recognizes. We have to proceed against a company which may be a shell, or in which the damage may already have been done, to a point where the action is almost meaningless. The individuals involved have a whale of an opportunity to get off scot free. It is that loophole that we are trying to plug.

Obviously, the big problem is that of dishonesty.

Senator TOWER. I understand what your motivation is, and I am confident that you would not administer this in an arbitrary manner and would be very sympathetic toward the operations of these SBIC's, but I think the very existence of this legislation—and my name is on it, although I have had some second thoughts about it—the very existence of this legislation, it occurs to me, might inhibit the individuals involved in the SBIC's in the exercise of sound business judgment.

In other words, it might be such an inhibition that our SBIC's would become pretty static operations, because of what they might be answerable for.

Mr. BOUTIN. I wouldn't think that that would be so, Senator. I think the National Banking Act is a very good example. I would not characterize our American banking system as being very static, and there the trustees or directors are subject to personal liability as well as employees, the same as we are recommending here.

Of course, we have other tools we could use, but they would not go against the individual. Violation of regulations, persistent violation, would be a cause for revocation of license, which effectively puts the SBIC out of business. Also, suspension of license, where the cause is less severe.

But it seems to me that if we are going to have regulations that we expect will be followed—and this seems to have been the common opinion of the various committees we have appeared before—that we should have good regulations; understood regulations, and enforce our regulations.

If we are going to do that, we must have a system whereby we can establish responsibility and guilt where guilt exists. I don't think—

Senator PROXMIRE. Would you yield briefly on that point?

The Administrator refers to the National Banking Act, and I have the appropriate section here. It says such violation shall however be determined and adjudged by a proper circuit district or territorial court of the United States. This gives the officer the protection of a court proceeding and all the protections that would enter into it, whereas the bill here gives the discretion to the Administrator. There is quite a difference.

Mr. BOUTIN. Well, of course, what we would have to do for enforcement, we would have to obviously bring suit, in most cases, for recovery. This would automatically get it into court.

Senator PROXMIRE. It would get into court, but the initiation would be yours, and the impact on the individual, and so forth, would be yours.

If we worded it this way, would you have any objection if we provided the judgment of the court, rather than the judgment of the

Administrator? Would you object to that, worded the way the National Banking Act is?

Mr. BOUTIN. Could I get our General Counsel involved, at this point?

I have said I am not an attorney.

Mr. ZEIDMAN, do you have any objection to the proposal of Chair?

Mr. ZEIDMAN. I would not think we have any objection to that at all. It was our intention in this language to make it clear that the determination by the court, as to liability, would also depend upon a determination by the court as to the violations in question.

Senator PROXMIRE. I am not sure that is responsive. Maybe it is, but what I was trying to get at was whether or not you would be willing to have this bill, which, as I understand it, now gives the discretionary action to the Administrator, changed to provide the following—let me read a couple of sentences:

If the directors of any national banking association shall knowingly violate or knowingly permit any of the officers, agents, or servants of the administration in any provisions of this title, all the rights, privileges, and franchises of the association shall be forfeited. Such violations shall, however, be determined and adjudged by a proper circuit, district, or territorial court of the United States and suit brought for that purpose by the Comptroller of the Currency, in his own name, before the association shall be declared dissolved.

In other words, you would have to bring the suit in court, in order to effectuate this, rather than simply act on your own and then bring suit to determine the specific liability.

Mr. BOUTIN. We would have no objection to that.

Senator PROXMIRE. Fine, Mr. Boutin. Now we are making progress. That is helpful.

Now, how about the requirement that personal dishonesty be a condition?

Mr. ZEIDMAN. If I may comment on your earlier raising of that issue, as I understand the bill to which you are referring, the Financial Institutions Act, out of which that language comes, that language referred to the basis for removal of officers.

Senator PROXMIRE. Correct. I think that is correct and I think maybe I should reserve that until we come to that particular section.

Senator TOWER. We might get some enlightening comments from the next witness on that.

Mr. Boutin, is this type of abuse and dishonesty in the SBIC's over the country?

Mr. BOUTIN. I wouldn't say that it is. I think that would be too broad a characterization, but we have a sufficient number of cases to indicate that it is serious.

Senator TOWER. I am just wondering if you aren't using a shotgun approach, when a rifle would be more utilitarian. I am very fearful that the bill, couched in its present terms, will be a very serious inhibition on participation by some very able businessmen.

Mr. BOUTIN. Of course I agree, Senator, that is a matter of opinion. I frankly think it will strengthen the industry. I think the fact that we have a law is going to make all the difference in the world in the industry's attitude.

Our attitude, as I have stated repeatedly, is one of wanting to see this industry grow and prosper and fulfill the mandate and the aspirations of the Congress.

We think it has got a long way to go to get there. If we can concentrate our efforts on working with and helping the good companies, rather than having to devote the bulk of our manpower to surveillance and police activities to get the mugs out who are in, and to keep others who want to get in out, I think the industry is going to prosper. I think it is going to fulfill the hopes that have been established for it, and it is going to make some money.

Senator TOWER. Would you be satisfied with a bill that is in substance similar to the Financial Institutions Supervision Act that we just passed in the Senate yesterday? Would that type of legislation give you what you need?

Mr. BOUTIN. Well, Mr. Tower, I am not really familiar enough with that act to really comment.

Senator PROXMIRE. That provided two powers. Sease-and-desist power and supplementary suspension and removal authority.

Mr. BOUTIN. I think that—

Senator PROXMIRE. Cease and desist now, as I understand it, the suspend and removal was suspended before hearing and removed after hearing. They only do it on the basis of personal showing of personal dishonesty.

Mr. BOUTIN. I think the tools that we have delineated in this proposed bill are the tools in all honesty, Mr. Chairman, that we need.

Now, I am not saying that every word is exactly perfect. We already, this morning, have talked about one change that is perfectly acceptable to us, but I don't think there is anything here that can be deleted, without us at SBA, being hamstrung in the performance of our duties.

Senator PROXMIRE. Let me just ask two more specific questions in this area, and I will try and be brief.

Assume an SBIC became capitally impaired, as a result of some bad, but honest, mistake in investments. Impairment constitutes a violation of your regulation. Would you consider the management of such an SBIC liable under this section?

Mr. BOUTIN. No.

Senator PROXMIRE. You would not. Don't you think the section should be redrawn to make that explicit and clear?

Mr. BOUTIN. I—

Senator PROXMIRE. See, if the violation of the regulation, and it specifies the violation of the regulation, you are in a position to act in such a way that liability can be pretty definite, as I take it.

Mr. BOUTIN. Let us take a look at that language and if it needs changing, Mr. Chairman, we will certainly be glad to do it. However, I certainly won't consider that a case for personal liability at all. That is not our intent.

Senator PROXMIRE. One more question on this section. Aren't we really concerned here about personal dishonesty? I think we brought this out. I think that that particular question has already been taken care of. I don't want to monopolize the questioning. I am sure the other Senators would like to question, either on this section or others, so, before I go into the others, suppose I yield to Senator Sparkman, if he would like to—

Senator SPARKMAN. Well, Mr. Chairman, you have pretty well covered some of the questions that I had in mind as I went through the statement.

Let me ask this, Mr. Boutin, because I think it is something on the positive side. Did I understand you to say that you were hopeful of coming up with a package that would provide certain incentives that we have been working on for some time?

Mr. BOUTIN. Absolutely.

For the next session of Congress, Senator, we will come up with a series of legislative proposals which will provide incentives. We are discussing, as the chairman said, with the Treasury Department right now possible alternatives that would provide tax incentives and other incentives in terms of financing available from SBA.

We are giving very close attention to the concept you have spoken of before, of a capital bank. We are giving serious attention to all of these things and will come up with some proposals to help bring success.

The legislative proposal we are considering this morning is to help us clean up the program, and then to keep it clean.

Senator SPARKMAN. In that connection, I noticed you referred to many companies that have done things that weren't right. How many SBIC's are there today?

Mr. BOUTIN. 686.

Senator SPARKMAN. How many of these are not in operation?

Mr. BOUTIN. If I remember, it is 82—105.

Senator SPARKMAN. 105 have died?

Mr. BOUTIN. Yes, sir.

Senator SPARKMAN. From one cause or another?

Mr. BOUTIN. Yes, sir.

Senator SPARKMAN. How many of these would have been saved, if you had had this law in existence?

Mr. BOUTIN. That is almost impossible—

Senator SPARKMAN. I realize that would be only an estimate you could give.

Mr. BOUTIN. It would be almost impossible to say. I will tell you, Senator Sparkman, I have spent so much time—

Senator SPARKMAN. Let me ask it this way: Would there be an appreciable number, do you think?

Mr. BOUTIN. Likely.

Senator SPARKMAN. I didn't mean to cut you off with what you wanted to say.

Mr. BOUTIN. I was going to say that I spent so much of my time in the last 90 days on the existing problem companies, I haven't had a chance to really go back and make a close analysis of those 105 that have dropped out and why they dropped out.

Senator SPARKMAN. Of course, I suppose a good proportion of those 105 surrendered their charters of their own volition?

Mr. BOUTIN. That is right.

Senator SPARKMAN. They found out it was not as easy going and as rich a land as they had thought.

Mr. BOUTIN. A little less gold in the hills than they thought. Many of them were minimum companies, too, very small individually owned companies.

Senator SPARKMAN. I think we are all probably somewhat sobered, in consideration of this legislation, by our experience in the recent bill that we had governing the financial institutions.

As the chairman has pointed out, a bill that came to us, that at first seemed to be quite noncontroversial, proved to have a good bit of controversy.

We had to make considerable change, before it finally went through.

Senator PROXMIRE. I think it is true of this bill, too.

Senator TOWER. Even more true, I think.

Senator SPARKMAN. I said our experience with that bill had perhaps sobered us in consideration of this bill. It seems to me that probably we would profit if, as we considered this bill, we would try to draw a parallel between what we did in the so-called cease-and-desist bill governing financial institutions in connection with these proposals.

I just throw that out as a suggestion.

Senator PROXMIRE. Very helpful.

Senator SPARKMAN. It might be well if someone, perhaps someone of the staff could do some comparative studies.

Senator PROXMIRE. Yes.

Well, I think, of course, because of the lateness of the session and because the administrator is very properly anxious to get action in both Houses on this bill, we will have to handle this bill in a way in which that part of it which is most controversial we will have to defer until next year. Otherwise it won't have a chance.

I suggest Mr. Barnes work with the SBA to see if they can develop that as quickly and effectively as possible.

Senator TOWER. Mr. Chairman, I would like to associate myself with that position. Whereas I have the highest regard for Mr. Boutin, we are creating some pretty broad instruments of power here that could have a stultifying effect, I think, on our small business investment programs.

Senator SPARKMAN. May I ask this question? I know you are trying to reorganize the SBA and are making some headway in it in order to get a more effective organization, a more efficient organization, but might not the abolition of the statutory status of the investment division be viewed as a downgrading of the SBIC program? Have you given thought to that?

Mr. BOUTIN. I have indeed, Senator, and I don't think this would be so at all. This would put it on a coequal basis with all of the other responsibilities of the agency.

Senator SPARKMAN. Is this the only one that has the separate—

Mr. BOUTIN. This is the only one. ID is the only division that is specifically mentioned in the statute. If anything, I would think the proposed change would elevate it because then it would be crystal clear that the Administrator is responsible—not some subordinate, but the Administrator. The program then rises and falls on his ability or lack of ability; his attention or lack of attention.

My own feeling is that in the past with the language as it has been, Administrators have felt that their hands have been pretty well tied because really the program was to be vested in this Deputy Administrator.

Now, I have not followed that philosophy at all, but nevertheless, from talking with people in the agency, I have been told that it existed.

I know that Mr. Ross Davis, who was Acting Administrator during the period from Gene Foley's resignation to my appointment, told me he had some grave reservations as to his power to direct this program because of this statutory language.

I think, too, that there is no need that I can determine anywhere for the retention of the language as it now exists.

Senator SPARKMAN. Now let me go back to something that you said in connection with a question the chairman asked, referring to the SBIC in Wisconsin, I believe. You said that all that a person had to do there was to call you or call the Investment Division and ask for advice. Now, had clearance been given, would he have been safe under the terms of this bill?

Mr. BOUTIN. Absolutely.

Senator SPARKMAN. Suppose, however, you advised against it?

Mr. BOUTIN. Well, first of all the condition would have to exist, Senator, that it would be a violation of law or regulation. On matters of law we would have no flexibility at all. The law speaks for itself.

On matters of regulation, we are the creators—the regulations are the creatures of the administration.

So we would then have every flexibility in the world to render an opinion or to give advice. So presuming now that in this particular case if a call had been made and they had been given the go-ahead by SBA, there clearly would be no violation of the law; no penalty.

If there had been a violation of the regulation and they had gone ahead anyway, then clearly there would be a question of personal liability.

Senator PROXMIRE. Would the Senator yield at that point?

It would seem to me an investment in a bankrupt company wouldn't comply with the provision of the law which requires that it be a sound loan and a secure loan, and under these circumstances if I were in Mr. Greenberg's position or in your position, I think I or anyone else in that position would be inclined to say don't do it. Play it safe. The law is pretty clear here and you shouldn't violate the law. In which case this company wouldn't have been saved and I think the big element of this whole program is that it is a risk program.

We have to expect people to make investments which are going to go bad because of the nature of the free enterprise system, that is going to happen. There are situations in which a company has had hard luck, as this one did, was bankrupt, but because they had the ingredients, good basic management and so forth, the SBIC wisely, as it turns out, went ahead with it.

It would seem to me that under these circumstances you are going to be stopping the kind, exactly the kind of risk investments which an SBIC should make.

Mr. BOUTIN. Well, of course, if this would be construed as a violation of the statutory provision that only sound loans be made, then it would not depend on violation of the regulation anyway, and the violation of the law would simply speak for itself.

We have many parallels. Take our own 7A business loan program. Congress has language in there that SBA must make a finding that there is reasonable prospect for repayment. Many of our loans go to companies which without the help of SBA would fold without any question. It is a matter of judgment.

Senator PROXMIRE. Well, at any rate you see why—I didn't mean to interrupt the Senator from Alabama—but you can see why this raises a question as to why we are so concerned about personal liability under these circumstances.

As you say, in many of these cases the company may collapse. In some cases they do. But with everybody playing it safe, we know the company will collapse and the SBIC won't be able to play the role it should play.

It is hard for me to understand why under these circumstances the directors and officers should be held personally liable to an extent that could be very great. These, after all, are wealthy men. If they will be able to contribute to an SBIC by and large it is unfortunate perhaps that you have to have people with money. But you do scare them out of the program by a personal liability provision, and you won't have a program that will work.

Mr. BOUTIN. Of course, what we are looking for here, is SBIC's to operate in accordance with the law and regulation. Where they are not willing to do that, I would rather they get out than to have us have the responsibility of bringing action in court to collect on the basis of personal liability.

But, if anyone in the program can't abide by the provisions of law and provisions of regulations, Senator, I don't know what they are there for. I think we have got to have some system of enforcement.

Senator SPARKMAN. I have only a couple more questions. One was this: Supposing that these people call in to clear their loans with you, aren't you inviting a terrific administrative load?

Mr. BOUTIN. Well, I didn't quite mean that. What I meant was any SBIC or the attorney of any SBIC or the official of any SBIC, where there was a question of doubt as to the provision of law or regulation and they wanted to discuss this with SBA, I think it is incumbent upon them to do so and it is incumbent upon us to give them a clear decision.

I don't think we want to open up a Pandora's box, certainly, of saying "now every borderline loan you make, you come in and check it with the Administrator." He doesn't have a personal portfolio that would indicate that they should have that kind of judgment, frankly.

Senator SPARKMAN. Let me ask just this last question. What is the effect of suspension of license?

Mr. BOUTIN. The effect of suspension?

Senator SPARKMAN. Yes.

Mr. BOUTIN. Well, the tool of suspension is intended to be used in those cases where there is an indication of future viability. Revocation, of course, is much stronger. Revocation effectively puts an SBIC out of business. Suspension means that simply that it can't operate; can't pay officers' salaries. It can only maintain the incidental expenses of keeping an office intact during the period of suspension during which corrective action can and should be taken.

Senator THURMOND. Mr. Boutin, how long have you been Administrator now?

Mr. BOUTIN. About 90 days.

Senator THURMOND. I want to commend you on your desire to make this a more effective agency and to prevent any corruption or dishonesty in it.

Mr. BOUTIN. Thank you.

Senator THURMOND. You have evidently given a lot of thought to it. I am just wondering about the recommendations that you have embodied in this bill. I presume they were made by some of your staff to you, from some people in whom you had confidence?

Mr. BOUTIN. That's correct. General Counsel, Mr. Greenburg, who is head of the program—

Senator THURMOND. I just wondered who you relied on chiefly.

Mr. BOUTIN. Actually, all of the top people in the Investment Division. General Counsel's staff Mr. Zeidman has been there for quite some time, Mr. Weimman, has also been there for some time, as has Roger Campbell, Assistant General Counsel for that division. Our Office of Economics, which has broad program responsibility has contributed. This effort had wide distribution within the agency. I don't know of a single instance of lack of unanimity of support for the provisions we are suggesting to Congress.

Senator THURMOND. Has anyone other than your own staff and counsel made any recommendations along this line that you felt worth considering and which you have embodied here?

Mr. BOUTIN. No.

Senator THURMOND. This has come from your staff, from their experience in working in the program.

Mr. BOUTIN. That is correct, sir.

Senator THURMOND. We are always a little concerned when we give more power up here because it is very difficult to keep power from becoming abused. It is important to have sufficient authority to properly administer the agency, and that is where we will have to try to walk the middle ground to determine just how far we can go to accomplish the purpose without granting undue power that later, although it might not be abused by you while you are here, someone else who succeeds you might abuse it.

Do you have any fears of anything along that line?

Mr. BOUTIN. No; I don't, Senator. I wish that I didn't have to be here this morning advocating legislation of this type. I would be remiss in my responsibilities if I didn't candidly tell this committee that the SBIC program; its regulation, its enforcement, its administration, has been—and I characterize this advisedly—in a chaotic mess. We need the tools to straighten it out if we are going to be responsive to the needs of the small business community and to the Congress. We have got to have tools to do the job.

We don't like this power. I am not interested in additional power for myself or any future Administrator. But I know that the Congress has every right to look down my throat if I don't do this job right and ask, "Now why didn't you do it? Why did you let these people get by with this stuff?" They have gotten by with plenty. So we are trying now to clean out the bad part of it. There is much that is very good and we intend to come up with new legislation in January to further strengthen the good part and concentrate on it.

I don't like the thought of having to bring someone into court and taking away any part of their personal fortune. But by the same token if they deserve it—if they have not administered a trust that was placed in them—then I think, by golly, they ought to pay for it.

The good ones, as I said in the statement, have nothing to fear. The honest people, the well-intentioned people, have nothing to fear.

We don't intend to enforce these provisions if we are granted this authority by the Congress in such a way that innocent people are going to get hurt. But the guilty people, I think, should be identified and held responsible. I think that is our whole system of Government in this country. I like that system.

Senator THURMOND. Thank you very much. That is all.

Senator PROXMIRE. I want to apologize for detaining you, but I want to ask two more questions of you. I know you will be brief and I will try to be.

One of our witnesses, Mr. Rollinson, will suggest an amendment to the act to provide procedures for the voluntary surrender of an SBIC license. I understand the staff sent you a copy of the amendment. Would you please comment on this?

Mr. BOUTIN. Mr. Chairman, I have not had an opportunity to study the amendment yet in detail, but I would like an opportunity, with your permission, to comment on the proposal for the record after I have had an opportunity to really go over it.

I would like to say, however, that as I understand it, it would permit a licensee to surrender its SBA license under certain circumstances but still to continue in business as some other form of financial institution. I don't believe that this provision would be in harmony with the purposes of the Small Business Investment Act. That act specifies that an SBIC shall be organized solely for the purpose of operating under the act. This is a fair warning to organizers and shareholders of the corporation that it can't be anything but an SBIC. The shareholders, the Government, and small business all have the right to expect it to operate as an SBIC. The organizers of an SBIC shouldn't be permitted to use this Government program as a stepping-stone to other pursuits if they find they do not want to remain in the program. They are free to leave it. We have provided methods by which this can be done simply and easily. But they shouldn't be allowed to leave the program with funds which they divert to other purposes.

I think it is a bad precedent to ask the Government to gear up for an investment in a program that the voluntary participants do not take seriously enough for a long-term commitment. The Government shouldn't be asked to play a game of "heads we win and tails you lose."

Senator PROXMIRE. Thank you very much. Now, that is helpful.

One last question and I only ask this because it is extremely important to the people in the industry. They are very deeply concerned about it. On page 13 of your statement you refer to section 4 of the bill which permits an examination by SBA of SBIC's portfolio companies. As I understand your statement, you seek this power to determine if there is a capital impairment of an SBIC. This would require a complete examination of the financial condition of the small business concerned and as I understand it, they are contending that this is virtually unprecedented and they feel that the small businesses which, after all, are only indirectly and in most cases very indirectly related to the Government, would feel that this was the kind of action they would deeply resent and it would very badly hurt the program.

Mr. BOUTIN. As I am sure the chairman of the committee knows, SBA presently has the authority, when an investigation is ordered by

the Administrator, to examine as part of that investigation a small business company. That automatically indicates an in-depth examination of all of the books, all of the records, discussion with personnel and so forth.

But what we are trying to do here, Mr. Chairman, is to provide a tool that can only be exercised with the personal, nondelegated authorization of the Administrator where upon examining an SBIC, if indications are that the information is less than factual, we can go to the small business concern or concerns where we think the information is other than what the SBIC made available to us, and we can then determine the facts of the matter.

This is not to be used on a daily basis. I don't have any idea how many times it would be used even in the course of a year. It wouldn't be used regularly.

Some of the companies, some of the problem companies where there is a serious question of bad information, bad records, would give us an opportunity, with statutory authority, directed by the Administrator, to go in and make an examination without an investigation. I think this is very prudent.

The alternative, of course, is that in cases where such a suspicion exists, the Administrator would have to order an investigation. This is a step that I would not like to use very frequently, sir. I think that the other is a much more prudent provision to use on an ordinary basis—not a frequent but an ordinary basis—and it is more serious, of course, to use the investigative provision.

Senator PROXMIRE. Well, now, the very least then, it would seem to me, that the kind of standards you suggest here should be written into the act so there would be more restraint.

The act provides that each small business concern which received financial assistance from an SBIC pursuant to that act shall in the opinion of the Administrator necessarily and appropriately be subject to examinations and so forth. It seems to me necessary and appropriate is hardly providing the kind of standards which would meet the criteria you would apply as you have described them here. This would require an extraordinary situation in which you feel that such an examination is essential and where the SBIC is in such condition that it would be necessary to proceed in this way.

Mr. BOUTIN. I think, Mr. Chairman—

Senator PROXMIRE. This is a wide-open provision here.

Mr. BOUTIN. I would entertain it as specifically authorized by the Administrator, placing it directly upon his back to exercise this authority wisely and personally.

Senator PROXMIRE. Mr. Boutin, I want to thank you very much. You are not only in the judgment of many people the top Administrator in the Government today, but you are certainly an excellent responsive witness. We very much appreciate your testimony on a highly controversial subject.

Senator SPARKMAN. May I ask one more question bearing upon your last question?

Speaking of standards of guidelines on that last point, as I understand it, now it just reads whenever the Administrator deems it necessary and appropriate.

Senator PROXMIRE. Necessary and appropriate, that's right.

Senator SPARKMAN. I wonder if there could not be some specific standards set there. In other words, that false information has been given, that would tend to impair the capital of the operations, or something along that line.

Mr. BOUTIN. We will be glad to work with the staff, Mr. Chairman and members of the committee, to try to develop better language that would be a better indication of what we are really trying to do here.

Senator PROXMIRE. That is exactly what I had in mind.

Mr. BOUTIN. We will be glad to do that.

Senator PROXMIRE. Thank you very much.

Mr. BOUTIN. Thank you very much, Mr. Chairman, and members of the committee.

Senator PROXMIRE. The next witnesses are Mr. Grogan Lord, Mr. Walter Stults, and Mr. Charles Noone of the National Association of Small Business Investment Companies.

We are all familiar with these gentlemen and very indebted to them for the fine cooperation and the great ability they brought to this program.

Senator SPARKMAN. Thanks for the training which they received in the Small Business Committee of the Senate. Both of them were on the staff of the Small Business Committee.

Senator PROXMIRE. I might say thanks to the training we have received at their hands since they have taken over here, and I am sure Mr. Lord has received the kind of training only a Texan can receive.

Senator SPARKMAN. Before you yield to our Republican friend, may I point out that Mr. Stults, for several years, was staff director of the Small Business Committee under my chairmanship even though he was a Republican.

Senator TOWER. Mr. Chairman, I have known Grogan Lord for about 20 years. I have seen him grow and develop as a business leader in my State and I think he is one of the most competent witnesses that we could have before this committee and I might point out he is not a Republican.

Senator SPARKMAN. This is a bipartisan presentation.

Senator PROXMIRE. Mr. Lord?

STATEMENT OF GROGAN LORD, PRESIDENT, NATIONAL ASSOCIATION OF SMALL BUSINESS INVESTMENT COMPANIES, ACCOMPANIED BY WALTER B. STULTS, EXECUTIVE DIRECTOR; AND CHARLES M. NOONE, GENERAL COUNSEL

Mr. LORD. Thank you, sir. Thank you, Senator Tower.

Mr. Chairman and members of the subcommittee, your continuing interest in the small business investment company program is heartening. I want to thank you sincerely for this second opportunity to appear before you this summer on matters that are of crucial consequence to our industry and the thousands of small businessmen that are dependent upon it.

As president of the National Association of Small Business Investment Companies, I want to thank you especially for this chance to testify on S. 3695. Our executive committee met here in Washington

over the weekend. The statement I am about to make has the full backing of the committee.

I want to begin with a few general observation on recent developments.

On July 15, less than 6 weeks ago, the chairman of this subcommittee encouraged the entire industry with his wholehearted affirmation of support for its objectives. The chairman, Senator Proxmire, speaking on the Senate floor, reported on the hearings concerning SBIC's over which he presided. He said they had "produced dramatic and persuasive evidence of the essential soundness and value of the SBIC program." He also said, "I am personally convinced of the great worth of this program and of the need for new and imaginative action on the part of the Congress and the executive branch to give the SBIC program the impetus it needs to accomplish the mission which we have assigned to it."

We are also encouraged, Mr. Chairman, by the statement in your newsletter that "we have come up with a number of improvements to get this SBIC program moving in a big way." Those words were music to our ears.

Similarly, SBA Administrator Boutin told this subcommittee on July 15 that he had spent 2 months studying the SBIC program and that he was "convinced that the small business community currently needs and will continue to need long-term loans and equity capital from SBIC's." The SBA Administrator said also, "I have seen much evidence that many SBIC's are making imaginative, needed contributions to sound progressive small business concerns." He also told the subcommittee that he felt that the program had "hardly begun to reach its full potential" and that "we must design our administration of the program so as to attract private capital and competent management."

July 15 was a good day for those of us who had wearied of assaults which lumped together the vast majority of honest and the handful of dishonest operators in the SBIC program. I left Washington certain that the highest priority was being given, to use Senator Proxmire's words, to "getting this program moving again."

Unfortunately however, legislation has been drafted and is before you which, appropriately enough, is supposed to help get rid of crooks. But the promise of positive action to bring more dollars and better people into the program has not been redeemed.

We support the aims of S. 3695, since we who are operating SBIC's have no less at stake in cleaning up our industry than does anyone else. On the other hand, we are concerned that our industry—if S. 3695 is enacted in its present form—may become the cleanest, and emptiest, in the whole Federal complex.

Look back a few years. The SBIC program was established because there was no institutional source of equity capital and long-term loan funds for small and new businesses. That was true in 1950 when Senator Sparkman put the first capital bank bill in the hopper. It was true when the 1958 act was passed. It is still true in 1966.

And I might add here it is more true in 1966 than ever before.

The fact is it's necessary to establish a balanced package of incentives and controls to bring private funds into this venture capital undertaking. I want to underline venture for the members of the committee.

The 1958 law gave certain incentives to encourage people to invest their personal dollars in this venture program. Subsequent amendments to the act in 1961 and 1964 changes the arithmetic some by raising the amount of matching capital funds under section 302(a). But those changes obviously did not provide the necessary leverage—I want to emphasize and underline also leverage—and there's still much more demand for SBIC funds than there is supply. The shortcomings of the present incentives are also apparent because more SBIC's and more dollars have been leaving the SBIC program during recent years than have been entering it.

There is an obvious need for greatly increased resources for the SBIC program. Yet SBA's statistics show that the total private capital of 637 SBIC's reporting to the agency on September 30, 1965, was \$434,600,000. That was less than the total of \$455,800,000 reported by 606 SBI's on December 31, 1962, almost 3 years earlier.

I'm afraid those two figures show that private investors have not been placing SBIC's very high on their hit parade. Equally important is the fact that a number of other SBIC's, large and small, are now on the way out, thus reducing the availability of greatly needed funds for smaller firms.

Our industry has had the support of Congress, SBA, and the administration. I'm convinced SBIC's can do a great job for the national economy. I'm sure money can be made in the program. But we must not overlook the fact that we're losing resources at a time when small business needs SBIC money more than at any time in my 30 years of experience with financial institutions.

We are here today discussing a bill that will give SBA many powers to police a handful of bad guys but will not give the agency one single dime to allow it to buttress and encourage good guys.

Let me be completely candid with you. Our executive committee thought long and hard about whether or not I should say these things to you. As you know, businessmen always say that everything's going great, that they have a waiting room full of clients or a portfolio full of AAA, high-interest securities. That's the tradition, and it may be bad form to break the hallowed rules of the game. But the truth is that the SBIC program is at a crossroads and if this subcommittee isn't able to help, the industry created by Congress—and which everyone seems to support orally—may very well expire.

The bill before you today contains 13 specific provisions granting new powers and authorities to SBA. We are pleased to note that some of these are directly responsive to suggestions we made to this committee on July 15. We support eight of the proposals without qualification.

But there are four provisions of S. 3695 which in their present form trouble us; namely, those authorizing SBA (1) to examine portfolio companies, (2) to remove officers and directors of SBIC's, (3) to impose a penalty of up to \$100 a day on SBIC's for late filing of reports, and (4) to place heavy financial liabilities on officers and directors of SBIC's. I want to speak about each of these proposals individually.

1. Section 4 of S. 3695 would add a new section to the 1958 act to permit the SBA Administrator to conduct examinations of small business concerns receiving SBIC financing. As far as I know, no other Federal regulatory agency or other instrumentality of the executive

branch, whether concerned with financial institutions or otherwise, has the statutory power to do this.

Granted, we are a unique industry in that we are eligible to receive direct injections of Government funds. But other industries concerned with financing receive comparable benefits from the Government in the form of guarantees and other types of subsidies. Yet the agencies regulating those industries have no statutory power to examine the books and records of their customers.

Banks and savings and loan associations benefit substantially from Government-supported insurance programs protecting their depositors. But neither the Comptroller of the Currency, nor the Federal Home Loan Bank Board, nor the Federal Deposit Insurance Corporation, nor the Federal Savings and Loan Insurance Corporation, has the statutory power to examine the depositors and customers of banks and savings and loan associations.

The Federal National Mortgage Association, which relies heavily on Government guarantees in its funding operations, serves as an important secondary market for mortgage funds for the housing industry. But FNMA has no statutory authority to examine the books and records of mortgagors.

We do not see any need for SBA to have such authority. If it is granted, many worthy small business concerns needing SBIC financing would avoid our industry, not because they had anything to fear but simply because they would want to forestall the prospect of being subject to time-consuming harassments at the hands of the SBA.

If the agency is concerned over possible criminal activities by portfolio companies of SBIC's or indeed any activity that might damage the agency or the program, we would not want to hinder its efforts to investigate those activities. But to examine individual portfolio companies where criminal activity is suspected, the SBA can go into court and get a subpoena or search warrant on a proper showing of need.

We urge the committee to strike this provision from the bill as an unnecessary depressant on an industry that above all needs encouragement.

2. Section 5 of the bill before would permit SBA to remove officers, directors, employees, and agents of an SBIC who are guilty of unlawful acts or omissions to act. We are in full sympathy with the purpose of this provision and we support it. In fact, it parallels closely our own recommendation to this committee on July 15 to give SBA clear authority to revoke SBIC licenses. But we believe that the procedural and due process safeguards in the bill as introduced are inadequate and we urge revision of the language to assure due process.

S. 3158, the Financial Institutions Supervisory Act of 1966, passed on Monday in the Senate, is designed in part to give Federal regulators authority similar to that now sought by SBA. But S. 3158 contains essential safeguards against the arbitrary use of authority by the Government agencies referred to in that bill. We feel strongly that procedural remedies and due process provisions such as those contained in S. 3158 should be added to section 5 of S. 3695.

3. Section 6 of the bill before you would add two new sections to the basic act. One of these would add penalties of up to \$100 a day for late filing of reports by SBIC's. As written, the provision is automatic and mandatory, leaving no room for avoiding the penalty, nor even authority for SBA to waive the penalty.

A minimum-size SBIC required to pay \$100 a day for the late filing of a routine SBA report would be hard hit if it were not permitted to explain the delay where it had good cause.

Other agencies have been given statutory authority similar to that sought by SBA in this bill, but in each instance there are provisions for showing cause.

The Internal Revenue Code sets forth penalties for the late filing of income tax returns and failure to pay estimated taxes and other delinquencies. But in virtually every instance the penalty can be avoided if it can be shown that the delay or failure is due to reasonable cause and not due to willful neglect.

The Federal securities laws contain penalty provisions of \$100 a day for late filing of reports with the SEC. But the Commission has the power to exempt a security issuer in whole or in part from such penalty if adequate cause for the failure to file on time is shown.

We believe similar provisions should be included in S. 3695.

4. Section 6 of the bill adds another new section dealing with the civil liability of officers and directors. Under certain circumstances, such persons could be held personally liable to SBA for all indebtedness owing to the agency. This is a harsh provision and one which we must oppose vigorously.

We think it important to examine the actual language of the provision to gain an appreciation of its impact. It provides in pertinent part:

Any officer or director of a licensee who knowingly participates, directly or indirectly, in a violation of this Act or regulation or orders thereunder relating to the disbursements of funds * * * by such licensee shall be personally liable * * * to the Administration (for) all indebtedness then owing to the Administration by the licensee * * *.

Let's relate that language to a major feature of our basic act with respect to SBIC loans.

One provision of the 1958 act, section 305(e), provides that:

Any loan made under this section shall be of such sound value, or so secured, as reasonably to assure repayment.

You will recall the first witness who appeared before this committee at the opening of its hearings on July 15. Mr. Donald P. Moen, president of Marathon Battery Co. of Wausau, Wis., testified that his company was in bankruptcy when he sought financing from an SBIC. The SBIC agreed to lend half a million dollars to the company provided Mr. Moen could raise an additional \$400,000 from a bank. Mr. Moen did so. The SBIC loaned the promised funds—and mind you, these SBIC funds were subordinated to the bank loan—and the rest was a success story.

Suppose Mr. Moen's company had not succeeded, and we were looking at this thing with "20/20 hindsight," after it received the SBIC funds. Suppose the SBIC had lost its half-million dollars. Under the bill before you, SBA might well have said that the loan to Marathon was not "of such sound value, or so secured as reasonably to assure repayment." That would have constituted a violation of the act. Every officer or director of the SBIC who participated in that decision to make the loan to Marathon would have been personally liable to SBA for any funds owing to the agency.

You will note that the same section fixes the liability of the officers and directors at the lesser of the amount lost by the SBIC or the

amount owing to the administration. This particular SBIC had \$700,000 in Government funds. If it had lost its own half-million although SBA had lost nothing, a liability would nevertheless have attached to each officer and director of that SBIC under the bill before you. And the liability would have been payable to the SBA which lost no money and not to the SBIC which had incurred the loss.

Surely, Mr. Chairman, you who hailed that case as an example of the good our industry can do would not want to make it impossible for that success story to be repeated.

We can find no precedent for such a provision in any other Federal regulatory agency. Granted, the Comptroller of the Currency has powers akin to those sought by SBA, but with two important differences. Under section 93 of title 12 of the United States Code, he may seek recovery from directors of national banks but only for violations of the statute itself and then only after such a violation has been determined and adjudged by a court. S. 3695 would impose a liability administratively, and apparently automatically, without any procedural safeguards.

The provision contained in this bill would impose an uninsurable liability on every officer and director of every SBIC. This, in our view, not only would utterly destroy the possibility of attracting desirable people to this program, it would certainly cause the many fine people now in it to leave.

Mr. Chairman, I cannot stress too strongly our opposition to this particular provision. It should either be stricken in its entirety or at the very least made to conform to the statutory authority vested in the Comptroller of the Currency and the language of the bill passed by the Senate Monday which limits officer removal to cases involving "personal dishonesty."

NASBIC also opposes the provision of S. 3695 which eliminates the statutory structure of the Investment Division within SBA. Ordinarily, internal reorganization is of little importance to anyone but the employees affected by it. Heaven knows, the Investment Division must have been reorganized at least a dozen times during the past 8 years and we never felt it worthy of comment. On the other hand, the basic change proposed by section 2 of this bill does pose a serious question about the future of the program.

As members of this subcommittee will remember, Congress, back in 1957, and 1958, considered putting the proposed small business investment company program either under the Federal Reserve Board or setting it up as an independent agency. At that time, the spokesman for the President urged that the SBIC program be put under SBA as a separate division. That was done and we believe it was a wise move. The Administrator of SBA had the power to name—and to fire—the Deputy Administrator for Investment and had unquestioned control over the Division's budget and other administrative operations.

On the other hand, the Investment Division maintained its responsibility for the SBIC program. It devoted all its efforts "to stimulate and supplement the flow of private equity capital and long-term loan funds" to small businesses, as directed by the preamble of the Small Business Investment Act of 1958.

Therefore, we hope that Congress will not reverse its 1958 action and risk losing the advantages which the statutory recognition have brought. We feel that the Administrator should have the powers of managing the Investment Division, as requested in section 3 of S. 3695, and it also appears sound to us for him to have one Deputy Administrator immediately under him to help him coordinate all aspects of his duties. We therefore ask that the statutory authority for the Investment Division be retained and that one Associate Administrator be named to supervise that Division, while it is made clear that the Administrator holds all necessary powers to administer and coordinate the operations of all units in SBA.

In summary, then, NASBIC supports S. 3695 with the changes I have mentioned. I shall be happy to leave with the committee suggested language incorporating the changes we propose your committee make in S. 3695.

I cannot conclude this statement, however, without emphasizing as strongly as it is in my power to do so that the encouragement we all felt this subcommittee concluded its hearings on the SBIC's has now been crushed by disappointment with the provisions of the bill that has been produced.

We are not quarreling with the aims of the control legislation. Not for one moment do we aline ourselves with sharp practices and ineptness that have been cited in hearings before this and other committees. But you will recall that in my previous testimony I asked the committee that in an effort to clean up the industry the baby must not be thrown out with the bathwater. What a tragedy that would be, for our industry is a healthy if troubled baby.

Let me cite testimony this subcommittee received last month. Former Deputy Administrator Richard Kelley, quoting from reports received and tabulated by SBA, told you that: (1) 33 percent of all businesses financed by SBIC's were new businesses, (2) small businesses financed by SBIC's showed an average increase of 86 percent in employment, (3) these portfolio companies increased their sales by 121 percent and their assets by 144 percent, and (4) perhaps most significant of all, the profits of independent businesses assisted by SBIC's jumped by 500 percent.

Another witness, Don Christensen of Greater Washington Industrial Investments, Inc., told you that his SBIC's portfolio companies registered an average increase of 370 percent in sales, a 780 percent rise in pretax profits, and 340 percent increase in net worth and a 107 percent climb in employment. This one SBIC accounted for 1,382 new jobs.

I don't know what better testimony we can bring Congress than the hard facts I have just repeated to show that SBIC's are doing a great job for small business. Going one step further, however, SBA data shows that SBIC's are not doing as well for themselves as they are for their customers. Our profits have been negative up until the last year and they are still far below what our invested dollars would be earning in thousands of other uses.

Now where is the legislation we had come to expect that would bring encouragement to the industry? Where is the legislation that would bear out the words of all those who stated in earlier hearings

their belief in the need to improve the leverage available to SBIC's? Where is the legislation that will bear out the statements during earlier hearings before this subcommittee that this is and should be a growth industry, needing further support to reach its "full potential"?

What we have here is a proposed law that is long on controls—some of them dangerously stifling, and probably ineffectual—and short on the kind of increased incentive that everyone says is needed. If there are plans underway to provide incentives later, then I must warn that the industry may well be strangled before it benefits from future plans to strengthen it.

We believe that this subcommittee should go beyond the provisions of the bill before it today and give us the help we need to realize the potential that has been cited here in Congress. On July 15, I gave you copies of a bill to amend the 1958 act which would go far along this road. Many of its provisions have been before you in years past; all of them are simple and follow the outline of the program as it has evolved.

This past Sunday, August 21, marked the eighth birthday of the Small Business Investment Act. These have been hectic years for a truly pioneering program. Please lend us tools we need to make it a significant instrument for strengthening the free enterprise system as Congress intended.

Thank you.

Senator PROXMIRE. I want to thank you very much for the strong and very effective analysis of the bill. Although you have found a number of places where you think the bill could be improved substantially, I am delighted to see that you do share our objectives and recognize we have to put a high priority on a bill that would help at least to achieve the objectives we all want, which is to eliminate the sharp practice and so forth from the industry.

Let me ask you specifically, on page 11 you say in referring to section 6 of the bill which provides the civil liabilities of officers and directors, you said it should either be stricken in its entirety or at the very least conform to the statutory authority vested in the Comptroller of the Currency and the language of the bill passed Monday, and so forth. As I understand it I think we got pretty much agreement from Mr. Boutin and Mr. Zeidman this morning that they would be perfectly willing to have it conform to the statutory authority vested in the Comptroller of the Currency in regard to this liability.

I would like to ask if you feel that at least we made that much progress and if you feel that would be acceptable. That would seem to square with what you are saying here. Do I interpret it correctly?

Mr. LORD. If we were operating in the SBIC industry under the same set of ground rules and under the same responsibilities as national bank directors and directors of Federal savings and loan associations as outlined under S. 3158 we would have no objection at all. All we want is the same set of responsibilities that every national bank director is operating under at the present time. We are just as much opposed to dishonesty as Mr. Boutin is and every member of the committee is.

Senator TOWER. Mr. Chairman, I think the ground has been pretty well covered here, both in our questions to Mr. Boutin and in Mr. Lord's testimony, and I think we are pretty well aware of what the

principal objection is to this bill. Mr. Lord, in private conversations you indicated to me, for example in your own company, that you felt that none of the principal participants could any longer participate under the provisions of the bill as presently written.

Mr. LORD. That is right, Senator. Under the way S. 3695 is written at the present time, I don't know of any directors in my company that could afford to take the chance on the responsibility as it is written.

Senator TOWER. Knowing his company, it is really a blue-ribbon list of prominent businessmen in central Texas. I think this is probably indicative of what would happen to a number of similar companies over the country.

Mr. LORD. At the NASBIC executive committee meeting over the weekend, there was not an SBIC represented there that didn't have the same set of facts and the same problem under S. 3695 as we view it in the Texas capital. When we have our director's meeting on September 15 at Austin, Tex., and our general counsel briefs our directors on S. 3695 and the way it is written and makes recommendations, I won't have a director left and I won't be one either.

Senator PROXMIRE. Now I think we have the same objectives and I am sure the administration has no intention at all of discouraging any of the people who are absolutely essential if this program will succeed. If we are to get a bill, it will take cooperation and compromise. This is why I would like to suggest that rather than simply leaving language that would be acceptable to you, that you designate the people whom you would have here in Washington who would work the SBA and with Mr. Barnes and Mr. Egenroad to try to work out acceptable language to the committee. Mr. Barnes and Mr. Egenroad can speak for us in that respect.

We have a couple of months left at most of the session and it is going to be terribly hard to get anything through even if it is not controversial and, therefore, we have to put something through that is acceptable to all interests and maybe that is the kind of bill we should have anyway but it is awfully important to get some of these provisions enacted and I would like to ask one other question in connection with this.

You say on page 7 in your very strong disagreement with the proposal to permit the SBA to examine portfolio companies, you say that to examine portfolio companies where criminal activity is suspected, the SBA can go into court and get a subpoena or search warrant on a proper showing of need. Apparently that is as far as you would like to go. You don't agree with the suggestion of Senator Sparkman which I think is sensible that you provide that standards to which the Administrator would be bound so that he would have under such extraordinary circumstances false information and so forth, the right to examine the portfolio.

Mr. LORD. Well, Mr. Chairman, you get into a lot of areas of judgment here. This is a judgment business. Our product is money. Our money is the same as all the other money out there. It is just that it is not available to these people. But this is a judgment business. Now in the judgment of the SBIC that made the Marathon investment it was a good one. That same judgment might not have prevailed in New York or California and that same judgment might not have prevailed by

this examiner that came into this SBIC 12 months, 6 months, 3 years after that loan was made. Whose judgment is it going to be?

In your loan agreement, in this private treaty, these negotiations that you have with these people who are customers of the SBIC, and they are customers of the SBIC, not the SBA.

Senator TOWER. In other words, in the development of risk capital, sometimes your judgment is vindicated and sometimes it is not. Otherwise it wouldn't be risk?

Mr. LORD. Right. That hindsight judgment is always much more sure than that front sight judgment. Here is what we are basically talking about. A legitimate small businessman comes to a SBIC and he needs money. You don't negotiate with these people without counsel. A good operating company will just not go into a term loan—remember our minimum term is 5 years. If you go in for 5, you better expect to be in for a minimum of 7 to 8 and probably 10, and in your loan agreement you have to set out as one of the conditions of making that loan to this small businessman that he gives blanket authority for SBA to examine his books at any time. If you don't include that in your loan agreement, you are signing that man in bad faith, if this bill passes; we don't have that now. I just can't imagine competent lawyers saying what does this mean? We say well we don't know what it means. That is when you are going to lose—

Senator PROXMIRE. In other words, it is specified that only where you have a situation where there is false information that has been filed or something of this kind, an extraordinary situation, where it is necessary for the SBA to make an investigation of portfolio companies if it is going to know what SBIC really amounts to because that is what an SBIC really is, it is largely the sum of the portfolio loans that it has, and unless there is some substantial understanding of what the individual small business companies are, there can be no adequate analysis of the SBIC. In some cases we found that these small businesses didn't even exist. They physically were a fiction. Unless the SBA has some authority to directly investigate, under extraordinary circumstances of this kind, it would seem to me it might be hobbled.

I don't want to press you fellows too hard but rather than shake your heads and say no, nothing, I think it would be helpful if you could come out with some kind of suggestion.

Senator TOWER. They have not said that. They have agreed to a number of the provisions.

Senator PROXMIRE. I mean in this particular area, you have indicated that the whole thing just ought to be thrown out.

Mr. SUTLIS. If there is any suspicion that you made a false loan, the SBA can order an investigation and under an order of investigation it can go to the small business concern. If they can't go there, SBA goes to a court and says, we have a valid order. We wish a subpoena. Now the court will give him that order if he shows cause. The real core of the problem we are discussing now is that this bill would change the ground rules. The talk was about impairment of capital. The only way they can carry out their own desires to know what kind of job we are doing and whether there is any impairment is to go to 20,000 small businessmen who have gotten our dough, look them over, make an evaluation and say yes, Mr. Lord, the evaluations that your

directors, under law, placed on this is reasonable, or no, Mr. Lord, it is not reasonable.

In the 1950's before this act was passed, there was a discussion of setting up a small business capital bank which would be run as a quasi-Government corporation. It was felt then that this was not a sound concept. The profit motive was a real good one to bring into this very difficult business. Under the 1958 act, we have private individuals who put up their own money and stand to lose that before Uncle Sam loses a nickel. Now this is the whole background and this is the reality.

Texas Capital has to lose \$10 million of its stockholders' money before Uncle Sam is exposed to a single dollar of loss. If the examiners of SBA want to go in and look at every portfolio company of Texas Capital or any other SBIC, they have got to say, we know more about how to evaluate a small business than does Mr. Lord and the board of directors.

Senator PROXMIRE. I am not asking that. I think that is right. You make a very legitimate point. I am saying there would be an extraordinary situation where there had been false information or where there is a reason to feel that the portfolio has been badly misrepresented, under these circumstances why not give, as defined, why not give them the right to move in. I can see if you have to go to court you might have to make such a showing and it might be tied up in the courts for quite a long period of time. And it might be impossible for the SBA to protect the capital that the Government has invested in it.

At any rate I would feel that I would hope that when you do confer with Mr. Egenroad and Mr. Barnes and the SBA on this thing that you won't just say that is out, I won't even discuss it. Consider some way of having at least in the most extraordinary kind of circumstances some opportunity for the SBA to protect itself.

Mr. STULTS. We would certainly like those safeguards written into law because as you know Mr. Boutin is our sixth Administrator not counting a couple of Acting Administrators. Mr. Greenberg is our fifth deputy not counting a couple of acting and each one of those men has different interpretations and rules.

Senator TOWER. I submit that although the judicial processes are slow, the reason for the existence of courts is to protect the citizen against the arbitrary will or judgment of one or a few people.

Senator PROXMIRE. I am just reacting to the investigation the McClellan committee had, that we had, the House Select Committee on Small Business had and I think we all agree we are not talking about Texas Capital or any of the outstanding SBIC's that would never be involved in this kind of thing but where you have a program that we hope will grow and get a lot more people into it. We can expect to have some sharpsters and we ought to have under these very extraordinary circumstances which you list in the law, an opportunity for SBA to protect the Government.

Mr. STULTS. I am not sure that if S. 3695 had been in effect 8 years ago that any of the McClellan cases would have been avoided. They involved faulty examinations and all kinds of shenanigans where men were just bound and determined to be crooks.

Mr. LORD. Think what would have happened if S. 3695 would have been on the books in the years past. You would have had those

105 problem, hanky-panky boys and as for the other 500 good guys, they would have been some place else.

Senator TOWER. What we are driving at Mr. Chairman, is we want to get the crooks but we don't want to drive the good guys out of the business. I think this is what these gentlemen are concerned about.

Senator PROXMIRE. We all agree.

Senator SPARKMAN. I just want to say that I think this is a very constructive statement that has been offered and we are indebted to Mr. Lord for making what I think are some very good suggestions for improving this legislation. And I feel confident we can work out a satisfactory bill.

Senator PROXMIRE. I would like to urge that you recognize the unfortunate time limit. We had hoped to schedule this hearing earlier but were unable to because the principal witnesses couldn't be here. If we are going to get action we hope in the next few days literally that you can sit down and start to work this out and we hope within a week or so you can come to some kind of conclusion.

It gives you a terrific opportunity to block things because it will take agreement on a bill which we will have to describe as noncontroversial if it will pass but as responsible people you have exactly the same objective we have and I would hope you could do that and work it out.

Mr. STULTS. Do you suppose we might work out a similar agreement on just a couple of little old incentive provisions and sneak that in unanimously, Mr. Chairman?

Senator PROXMIRE. It would be wonderful if you could. But at the same time the budget and SBA have their deep concerns about the details of an incentive bill. They want to take a little more time. Just as it is possible for you to block this it is possible for them to prevent action on the other side.

I think you would all agree that this kind of action provided you can agree to it to prevent the kind of fraud and so forth which has occurred should have clear sailing and right now we hope we can get the kind of force behind the incentive bill you describe.

Senator SPARKMAN. You heard, I presume, Mr. Boutin's definite promise that legislation would be presented in January.

Mr. STULTS. Yes, sir; I heard the promise.

Senator SPARKMAN. That is better than we ever had before.

Senator PROXMIRE. And then the SBA is, right now, talking, we feel, constructively and making progress with the Treasury on the incentives in the tax bill. It has been a long time since they were communicating this way but I think they are now at last. I think they are beginning to understand each other and we will be able to get some real—

Senator SPARKMAN. I take it from Mr. Boutin's statement that they are close enough that he felt safe in making a definite promise that legislation would be presented to Congress this January.

Senator PROXMIRE. I would endorse that. Any further questions?

Senator TOWER. I have no further questions.

Senator THURMOND. No questions.

Senator PROXMIRE. Mr. Lord, I want to thank you very much.

There are other witnesses here. We have permission to continue to meet and if Mr. Rollinson and Mr. Christensen would like to testify now, fine. Otherwise they can appear tomorrow.

STATEMENT OF DON A. CHRISTENSEN, PRESIDENT; AND MARK ROLLINSON, VICE PRESIDENT AND HOUSE COUNSEL, GREATER WASHINGTON INDUSTRIAL INVESTMENTS, INC.

Senator PROXMIRE. You gentlemen have been very helpful to us.

Mr. ROLLINSON. Thank you. Mr. Christensen will lead off.

Senator PROXMIRE. Mr. Christensen will make the presentation; is that correct?

Mr. CHRISTENSEN. Yes, sir.

Mr. Chairman, Mr. Rollinson and I are appearing today as representatives of Greater Washington Industrial Investments, Inc., for the following purposes:

First, we desire to support S. 3695 except with certain reservations we have as to sections 4 and 5 of the proposed bill; and secondly, and more importantly, we desire to submit for the committee's consideration a proposal which would permit the voluntary surrender of an SBIC license upon satisfaction of certain standards. With your permission, I should like to give you our comments with respect to S. 3695 and to outline in general the reasons why we believe provisions for voluntary surrender of an SBIC license will properly round out the regulatory pattern. Mr. Rollinson will outline more specifically the mechanics of our proposal and its consistency with similar regulatory programs.

I. COMMENTS ON S. 3695

I consider it essential that Congress give SBA whatever additional legislative authority it needs to effectively administer the program, and in that respect I concur fully with the purpose of the proposed bill. Unfortunately, however, certain provisions of the bill go beyond what I believe SBA needs for an effective enforcement program and consequently impose unnecessary additional burdens on legitimate SBIC's such as Greater Washington. I am particularly concerned with section 4 of the bill which introduces SBA examinations into our heretofore private contractual relationship with independent portfolio companies and with section 5 which appears to increase significantly the personal risks in being a Greater Washington director.

(a) *Section 4*

In competing for the better investment opportunities we often have to assure prospective investees that they are contracting with us as a private company and that they will not be subject to the additional Government controls or examinations which typically are associated with Government loan programs. I believe the proposed section 4 would clearly put us at a competitive disadvantage relative to the other sources of capital available to such businesses, and if it cannot be eliminated entirely, I would hope that it could at least be limited to those portfolio companies which (a) represent an investment of more than 10 percent of the SBIC's capital, or (b) are under control of the SBIC, or (c) are in default under the terms of their agreement with the SBIC.

(b) *Section 5*

I believe the increased personal liabilities imposed by section 5 will also put us at a competitive disadvantage by making it considerably

more difficult to recruit and retain responsible outside directors. Even as a full-time SBIC operator, I personally have difficulty in keeping abreast of all SBA regulations, and it is unrealistic to expect my outside directors to be able to devote the attention which is necessary to protect themselves from liability under this section. Since most of GWII's directors serve in a quasi-public service capacity—rather than as significant shareholders in their own right—they have little incentive to incur the risks these provisions represent. Consequently, I would hope that such outside directors at least could be exempted from the provisions of sections 313(a) and (e) and further, that the application of these sections to others could be limited to those violations which are willful and of material importance.

In addition, I am concerned as a layman that the language proposed in section 313(b) might be susceptible to such broad interpretation as to preclude the risk-taking type of venture capital investments which we thought Congress intended SBIC's to make. I would hope, and it is clear from your statements this morning, that this is not the committee's intent.

II. PROPOSAL FOR VOLUNTARY SURRENDER OF SBIC LICENSE

(a) Suggested legislative amendment:

We propose that the following section be added to the Small Business Investment Act:

VOLUNTARY SURRENDER OF LICENSE

Sec. 317. A Licensee may surrender its license at any time provided such Licensee—

- (a) is not indebted to the Administration directly or through a loan guaranty;
- (b) submits an undertaking to the Administration or, in the case of a Licensee which is also a registered investment company under the Investment Company Act of 1940, to the Securities and Exchange Commission, in form and substance satisfactory to the Administrator, to specialize, for a period of 3 years, in investment in small business companies which qualify for investment by Licensees as defined by Administration Size Standard Regulations as of the date of this amendment;
- (c) has presented the matter of surrender to its shareholders and has received an affirmative vote of more than two-thirds of the Licensee's outstanding stock;
- (d) has submitted to the Administration in writing at least six months in advance of the proposed surrender date a certified copy of resolution of the Licensee's Board of Directors whereby the Board recommends to shareholders the proposed surrender; and
- (e) is not involved in any proceeding under Section 309, 310, 311, 312, 313, 314, or 315 of the Small Business Investment Act of 1958 as amended.

The above legislative proposal permits those SBIC's which have matured to the point where they can operate without Government funds and without the special incentives of the SBIC program to "graduate" from the SBIC status by surrendering their license and foregoing future Government support. They would, however, commit themselves to a continued investment program in small businesses, but without the many regulatory constraints which now limit flexibility. Such postgraduate SBIC's, I believe, would represent tangible evidence of the success of the SBIC program and would reflect credit on the Congress and this committee for its achievement in creating a viable new financial vehicle.

Greater Washington, like many of the other publicly owned SBIC's, is basically a venture capital operation, investing in young and rela-

tively unproven companies which in our judgment have the potential for significant future growth. We originally attempted to model our operation after American Research and Development Corp., the first, and still the largest, publicly owned venture capital company. In its 20 years of operation, ARDC has made a fine record. Its net asset value has increased from \$8 per share at inception to more than \$43 at June 30, and this is in addition to cumulative distributions to shareholders of \$6.65. Although ARDC is not licensed under the Small Business Investment Act, it serves small business as effectively as any SBIC I am aware of. It should be noted that this is not because it is required to by regulation but rather because it sees a principal economic opportunity there.

Similarly, there are other established private venture capital companies, also not licensed under the act, and they too invest principally in small businesses, again because they see the greatest opportunity there. Without using Government funds or employing the other special incentives available to SBIC's, these firms have created viable venture capital operations which fully serve the Congress' purposes in establishing the Small Business Investment Act. I believe many of today's SBIC's can ultimately achieve the same position.

GWII has been an active supporter of the SBIC industry. I personally served as a governor of our national trade association for 2 years and Mr. Rollinson is now in his second year as treasurer of the regional association. We have both participated in various industry studies, including the present CED work, and we have worked diligently with SBA and the other Government regulatory bodies in developing their regulations for SBIC's.

In short, we believe in the purposes of the program and are dedicated to see it succeed. However, from our point of view, full success of the SBIC program will have been achieved only when SBIC's are sufficiently strong and viable to operate without Government subsidy. In other words, we see the SBIC program as a mechanism for creating, by providing Government sponsorship during the formative years, what ultimately will become totally private small business investment companies. Today, I believe some of the public SBIC's may be able to make that transition; however, there is presently no incentive for them to give up Government funds and there is no method for them to graduate from the program.

Public SBIC's presently are intensively regulated. They must operate under what often become a conflicting set of regulations, imposed by SBA in administering the 1958 act, by SEC in administering the Investment Company Act of 1940 as well as its other securities acts, and by IRS in administering the tax laws. Consequently, I believe the most effective incentive that Congress can offer SBIC's to encourage them to give up their Government subsidy is the elimination of one level of this regulation, namely, that by SBA.

Clearly, the Government's interest in the SBIC program must be protected, and this requires regulation. However, I believe there are really two different interests which justify two different approaches; the first is the Government's interest arising from its dollar investment in the program, and the second is the Government's interest in seeing that small business has available to it a continuing source of long-term debt and equity funds.

It would appear from the testimony given in the recent congressional hearings by the Comptroller General and by the SBA Administrator that effective protection of the Government's creditor interest will require SBA to take a more active role in directing an SBIC's day-to-day operations. The Comptroller General's strong recommendations regarding investment criteria will do just this, and his implied criticism of new venture financing may well necessitate SBIC's adopting more conservative investment policies.

Similarly, it appears from GWII's own experience in currently attempting to obtain loan funds from SBA that disbursement of such funds will require specific justifications of their use, possibly even to the extent of SBA passing judgement on the credit worthiness of the particular small businesses to receive them. This contrasts sharply with the previous policy whereby such funds were advanced in a lump sum for use by the SBIC at its discretion in making small business investments. Although these policies may seem justified in protecting the Government's interest as a creditor, I believe they go beyond that and represent a potentially serious encroachment on SBIC management prerogatives. This is particularly burdensome for the venture capital-oriented SBIC which needs operating flexibility above all else.

I would now like to have Mr. Rollinson comment briefly on the explanation of our proposed amendment.

(c) Explanation of proposed amendment

Mr. ROLLINSON. Mr. Chairman, let me say at the outset that we are sorry time didn't permit us to suggest language which would incorporate Mr. Christensen's suggestions regarding sections 4 and 5 of S. 3695. We are prepared to do so later.

Senator PROXMIER. If you can do that this afternoon or tomorrow we would be delighted to have it. The committee will be in session tomorrow.

Mr. ROLLINSON. I see.

The proposed amendment we have submitted here today is intended to offer an alternative other than liquidation, whereby an SBIC may surrender its license and be relieved of SBA regulation if the SBIC undertakes to remain in the business of specializing in offering long-term debt and equity financing to small business.

As a general proposition, Federal licenses are purely voluntary both in inception and duration. The only exception involves those licenses which carry with them quasi-monopoly privileges and responsibilities, usually granted in the form of "certificates of public convenience and necessity," which exclude as a matter of law all unlicensed competition. Common carrier franchises are the most notable exception.

Nor is it unusual for a licensing statute to assure the right of voluntary surrender of the license (e.g. as to Federal Reserve banks, 12 U.S.C. 329; Federal savings and loan associations, 12 U.S.C. 1464(i); national banking associations, 12 U.S.C. 214(a)). All enjoy this right as a matter of statute, not as a matter of regulatory authority.

Presently, if an SBIC determines that the disadvantages of the program outweigh the advantages, the only way out, under the regulations, is liquidation (107.205). I refer you to section 205 of the small business regulation under the act. This regulation was promul-

gated by SBA after one SBIC had voluntarily surrendered its license and more surrenders appeared to be on the horizon.

I might note parenthetically that that one voluntary SBIC surrender involved a company which had some serious internal problems and it may have been suspected at SBA that the reason for the surrender was that they were trying to prevent SBA from enforcing some of the regulations as to problems that had come about in the way of violations.

The amendment we propose has the salutary effect of tending to keep private funds committed to the assistance of small business—funds which otherwise might be dissipated through liquidation.

I point out to the committee that roughly 25 percent of the private funds in this industry are committed to liquidation today.

Senator PROXMIRE. Say that again, Mr. Rollinson.

Mr. ROLLINSON. It is my understanding that roughly 25 percent of the private funds in this industry are committed to liquidation today. I believe over \$100 million of private funds are committed to liquidation.

Senator PROXMIRE. How many SBIC's are included?

Mr. ROLLINSON. It is a relatively small number. I can't recall—under 25.

Senator PROXMIRE. Several very large ones apparently.

Mr. ROLLINSON. That is true.

Senator PROXMIRE. Are committed to liquidation. You mean publicly announced?

Mr. ROLLINSON. Yes, sir.

Mr. CHRISTENSEN. Or have completed it already.

Mr. ROLLINSON. Or have already gone through it. A few have. It is difficult to do. There is a lot of redtape to go through, but clearly they have announced that intention. These are the professionally managed companies, the larger ones.

Senator PROXMIRE. Includes Marine Capital of Milwaukee?

Mr. ROLLINSON. Yes, sir; it does.

The salient features of the proposed amendment are as follows:

NO DEBT TO SBA

The licensee must not be indebted directly or through loan guaranty to SBA.

UNDERTAKING TO SPECIALIZE IN SMALL BUSINESS

The licensee must submit an undertaking to continue to specialize in small business. The undertaking must be in form and substance satisfactory to SBA; that is, it must contain agreements to submit to SBA auditing and enforcement powers to the extent necessary for SBA to police and enforce the undertaking so as to protect all parties concerned, including small business concerns in the portfolio and licensee's shareholders.

SHAREHOLDER APPROVAL

Two-thirds shareholder approval, required by the proposed amendment, is that degree required for charter amendment by most States' corporation laws. Approval of licensee shareholders must be obtained, after submission to shareholders of all relevant facts.

For companies registered as investment companies under the Investment Company Act of 1940, this will automatically mean the additional full disclosure required by Federal securities laws, under SEC supervision, of the effects of surrender of the license.

SIX-MONTH NOTICE TO SBA

Notice to SBA, prior to surrender of license is modeled after the 6 months notice requirement of the Federal Reserve Bank before a bank can withdraw from Federal Reserve membership (12 U.S.C. 329).

The primary purpose of such a provision would be to allow SBA ample opportunity to audit the SBIC's affairs to make certain that the SBIC is not merely surrendering its license to attempt to remove itself from SBA jurisdiction over past violations.

The notice provision, combined with the undertaking to continue to specialize in small business investment, also provides SBA with ample opportunity to encourage new licensees in the surrender area, if that is deemed necessary or desirable.

NO PROCEEDINGS AGAINST LICENSEE

The proposed amendment would require that there be no proceedings of any nature under the act against the licensee at the time of surrender. This insures SBA jurisdiction for as long as is necessary to remedy any violation or other difficulties that may have arisen during the course of the licensee's business.

That concludes our statement.

Senator PROXMIRE. Fine. Mr. Rollinson, I think you have indicated that you found that SBA regulations are overly stringent or unclear. Would you care to comment in detail upon that?

Mr. ROLLINSON. Yes, sir. There is no single SBA regulation that is so onerous in itself that we can say "this must be changed," or "this is very bad." Collectively, these regulations hamper our activities and flexibility tremendously.

Let me give a few examples. We have a regulation which is designed to prevent cross dealings between SBIC's. It is drafted so comprehensively that we find that when we do a participation with another SBIC we are unable to make a supplementary investment in the portfolio company after that date.

Senator PROXMIRE. Have you under these circumstances discussed this with the SBA people and—

Mr. ROLLINSON. We certainly have.

Senator PROXMIRE (continuing). And try to see if they would waive it somehow or work out a way to accomplish this?

Mr. ROLLINSON. Almost all these problems are things that you can apply to SBA for an exception on but this takes a great deal of time and frequently there isn't that sort of time available. This is a fast moving business and one is not amenable to the bureaucratic process. It just doesn't work.

In addition we have commented in great detail on all proposed regulation except the most trivial and this one is certainly no exception. We have spent a great deal of money in legal fees and in our own time in trying to make constructive comments.

Senator PROXMIRE. To the SBA?

Mr. ROLLINSON. Yes, sir.

Senator PROXMIRE. To the Administrator and to the head of the Investment Division and so forth.

Mr. ROLLINSON. Yes, sir.

Another example is of a conflicting regulation, and there are several of these. Let me give you an example. One of the primary advantages to us is a tax advantage that has nothing to do with being an SBIC and that is we are a regulated investment company. The SBA regulations are such that it makes it much more difficult for us to take advantage of the tax incentives of being a regulated investment company.

For example, as a matter of statute, most of our losses are ordinary losses. For a regulated investment company in the venture capital business, an ordinary loss is the least desirable kind of loss to have. You are not allowed to carry them forward as an operating company is, whereas capital losses are, can be carried forward to future years. When we have a loss it is usually large. Our ordinary income is very small. We are not a high-interest operation, but low-interest operation.

So we have no income against which to offset these ordinary losses. These conflict and make it more difficult.

I would say that being a regulated investment company is the only positive incentive we have as being an investment company and it has nothing to do with being an SBIC.

There are some of the size standards regulations that are inappropriate for an industry. This is not a real burden and less than 1 percent of the deals we look at are hampered by this. Occasionally there is an industry in which a size standard is out of order; they must be higher in some industries because if the company is to compete with giants, clearly the standards must be different than for the corner haberdasher. These are different standards.

We are having a number of problems relating to unwitting violations. These are violations that make this proposed regulation a little bit difficult. For example, we may invest in a company which has a shareholder who is related by blood to one of our directors and our director may not know this, may not even know his cousin or uncle is a shareholder in that little company. That is clearly a violation of the SBA regulations. We would never know this. We might make an investment and not know this.

The legislation that we have here today is such that it is my legal opinion that such an investment would automatically make our directors personally liable for any indebtedness to SBA even though it was totally unwitting. It was intentionally making the investment I believe that the act speaks of.

There are restrictions as to the type of industries in which we can invest. Things that are farm or farm related industries are prohibited to us. There are some agriculturally oriented high technology manufacturing businesses which would be of interest to us, that possibly are prohibited under present regulations. There are restrictions that have to do with who our officers and directors are, whether or not they are experienced and whether they meet SBA standards.

I think these are probably appropriate but again these are restrictions that force us to depend on the man, the administrator, not on the law.

We have overregulation and then we say "here we have a benign bureaucrat who is going to give exceptions to each of these things." Sometimes he is a benign bureaucrat and sometimes he isn't.

Senator PROXMIRE. Depending on whether he gives you the exception or not.

Mr. ROLLINSON. Yes, that is right.

Senator PROXMIRE. I will tell you, this is very, very interesting. I wish when you go over your remarks if you would like to supplement them or send in additional memorandums because I would like to have an opportunity to study this and discuss this with some of the SBA people.

Mr. ROLLINSON. We would be pleased to.

Senator PROXMIRE. And with some of our staff. Would either of you gentlemen care to comment on the explicit reply which the Administrator gave to your proposal here this morning when he said that he felt you ought to either be in the program or out of the program and this would not serve the public interest in continuing the status you describe here?

Mr. CHRISTENSEN. The program as presently constituted is based very heavily on the use of Government funds.

Senator PROXMIRE. On use of the Government funds?

Mr. CHRISTENSEN. Yes. The regulations that are developed are really designed to regulate and protect the Government's creditor interest. It is my feeling that eventually SBIC's ought to be able to become viable, independent companies not needing Government funds and not needing Government subsidies.

Thus I believe that there should be a way of graduating out of the program and out of the regulations that are really designed to protect the Government's financial interest.

Now it is my feeling that the provisions we are suggesting here would preserve the Government's interest in seeing that we invest in small business. This is what we would like to do.

Senator PROXMIRE. Supposing after you get in this position instead of investing in a small business firm you put it in a larger firm. There is every incentive for that because if you invest \$2 or \$3 million at a time it is a lot more economical than to make 20 or 30 hundred thousand dollar investments. Not in all cases but in general. You only make one investigation, for instance, instead of 20 or 30.

Mr. CHRISTENSEN. Two reasons. One, as part of our procedure that we described here you undertake in a form and substance satisfactory to SBA to continue to invest in small business. In other words, this is not to go away.

Senator PROXMIRE. Undertaking must be in a form and substance satisfactory to the SBA?

Mr. CHRISTENSEN. That is right.

Senator PROXMIRE. You would require that this also be specified, that you agree to continue to invest in small businesses?

Mr. CHRISTENSEN. That is correct.

Senator PROXMIRE. For how many years?

Mr. CHRISTENSEN. We have set it up here as 3 years.

Senator PROXMIRE. Why?

Mr. CHRISTENSEN. There is nothing magic about the 3-year term. We thought it was not appropriate to make it—

Senator PROXMIRE. Why wouldn't it be desirable to make it permanent or to provide that as long as you weren't required to liquidate. In other words, you would have the opportunity to either liquidate or to invest in small firms. The whole point of the program is to get money invested into small business and I know that Mr. Rollinson was shaking his head a minute ago when I mentioned the desirability of the big investments instead of the small investment. That is the whole reason for this program. That is why we have to have SBIC's. If small business investments were this attractive we could forget about all this legislation.

Mr. ROLLINSON. I was looking—and I don't have it with me—for American Research Development's report. We have a company that specializes in investing in small business.

Senator PROXMIRE. A few people have done this. Eberstadt & Jelke, I think, had this kind of operation. But they have been rather few and there still is the fact that one investigation after another by Government, by industry, by universities, have indicated that small business has terrific trouble getting this kind of long-term capital. It is just not that easy and there would be a tendency, it seems me, if there weren't some kind of carefully spelled out provision for you to get out of small business investments into big. I like the part that I am sure you skipped reading in the interest of time but where you say it must contain agreements to submit to SBA auditing and enforcement powers. That would be the SBA would be in a position to make sure your investments were bona fide small businesses.

Mr. CHRISTENSEN. That is correct. The American Research Development Co. was a company with a stated net worth of \$66 million. You go through their portfolio and at least 95 percent, possibly more, of their investments have been in small businesses. The reason is that they see the economic opportunity there in the young, growing business and they are technologically oriented, the same as Greater Washington is. There is a prime case of not being interested in going out and investing in blue chips or big companies. We see our opportunity here and we see the small business investment program as the way of getting companies such as Greater Washington started creating them and encouraging their formation so eventually they can become strictly private American research and developments.

Senator PROXMIRE. Well, as you know, this is not a new proposal and it is one that has been considered for some time. It does seem to have, I think, a considerable amount of merit because after all our objective is to get long-term capital into small companies but I do think that we have to give it consideration next year because we are pressed and we can only put the most acceptable kind of provisions through the Congress now and SBA very strongly opposes this. I am glad you brought it to our attention. It is a real service to do so.

We maybe ought to get some more explicit answers. I think the Administrator himself, who is a very competent man, indicated this morning he wanted to do this. He hadn't had a chance in the short time he has been Administrator to consider it in detail.

I want to thank you gentlemen very, very much, and I don't want to imply by my questioning that I confine my comments to the one specific approach you made at the end. I think some of the other sug-

gestions you made are very good. Your emphasis that the Congress needs to recognize this must be a risk program, not run simply as the Comptroller General's reports would imply to eliminate all risk and, therefore, make it a banking operation. It must be a risk program. I think that is a very healthy and wholesome contribution.

Mr. CHRISTENSEN. The Comptroller General's report is disturbing to firms such as ours.

Senator PROXMIRE. If you didn't make bad investments occasionally, you wouldn't be doing your job.

Mr. CHRISTENSEN. That's right.

Senator PROXMIRE. You have to have a record, it seems to me, over the years, of a series of companies that just don't make it. Otherwise, you aren't investing and providing risk capital. This is what risk means.

Mr. CHRISTENSEN. Every indication of the regulatory attitude that is developing, though, is one which will constrain us more.

Senator PROXMIRE. Sure. That is a natural thing, and it is up to us to try and reconcile that and to try to persuade the SBA to recognize the very great importance of providing administration and us to provide the laws that will encourage risktaking. I understand their view, too. They get criticism from the Congress and the papers on money that has been lost and they have to answer for it, and it is very tough for them.

We thank you very much.

These hearings have been most constructive this morning. We will stand adjourned until 10 o'clock tomorrow, when we will hear Senator Harris.

(Whereupon, at 12:40 p.m., the subcommittee was recessed to reconvene at 10 a.m., Thursday, August 25, 1966.)

SMALL BUSINESS INVESTMENT ACT AMENDMENTS OF 1966

THURSDAY, AUGUST 25, 1966

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

The subcommittee met at 10 a.m. in room 5302, New Senate Office Building, Senator William Proxmire (chairman of the subcommittee) presiding.

Senator PROXMIRE. The subcommittee will come to order.

Our witness this morning is Senator Harris from Oklahoma. Senator Harris, we are delighted to have you here. You did a fine job in chairing the hearings of the Permanent Investigations Subcommittee and looking into the SBIC program just a couple of weeks ago.

Senator HARRIS. Thank you.

STATEMENT OF FRED R. HARRIS, U.S. SENATOR FROM THE STATE OF OKLAHOMA

Senator HARRIS. Thank you, Mr. Chairman. I'm happy to have the opportunity to appear to testify in support of S. 3695, introduced by you, Mr. Chairman, and joined in by Senators Sparkman, Tower, Mundt, and myself.

Senator McClellan, who is chairman of the Government Operations Committee, which under the Legislative Reorganization Act of 1946, has the duty to look into the efficiency and economy of programs adopted by the Congress with a view toward making recommendations for administrative and legislative changes asked me to serve as acting chairman of the Senate Permanent Investigating Subcommittee of that committee to hold some hearings into the operation of the small business investment company program.

As the chairman knows, we held rather lengthy hearings extending over 3 full days with representatives of the Small Business Administration and the General Accounting Office who had made some investigation into the operation of this program at our request and some of the individuals who had been involved in companies which had experienced severe difficulty.

I joined with you, Mr. Chairman, in cosponsorship of S. 3695 because it embodies by and large the tools which Mr. Boutin of SBA suggested that he needed in order to make corrections in the admin-

istration of that program. In addition to that, our staff, Mr. John Walsh and Mr. Jerry Adlerman on the Investigating Subcommittee, prepared another bill and it has not been introduced yet, but I would like to offer it for the record in this hearing and respectfully suggest that it might be considered along with S. 3695 for inclusion of all or a portion of its provisions in whatever legislation this committee might eventually decide upon.

Senator PROXMIRE. Without objection, the copy of that bill will be printed at this point in the record.

(The bill follows:)

[S. —, 89th Cong., 2d sess.]

A BILL To strengthen certain provisions of law relating to the organization, operation, and supervision of small business investment companies

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

LIMITATION ON BORROWED PRIVATE CAPITAL FOR SMALL BUSINESS INVESTMENT COMPANIES

Section 1. (a) Section 302(a) of the Small Business Investment Act of 1958, as amended (15 U.S.C. 682(a)), is amended by striking out the period at the end of the first sentence and inserting in lieu thereof the following: “, and not to exceed 33 $\frac{1}{3}$ per centum of such paid-in capital and surplus shall consist of borrowed funds.”

(b) The amendment made by this section shall not apply to any small business investment company licensed under section 301(c) of the Small Business Investment Act of 1958 prior to the date of enactment of this Act.

SAFEGUARDING OF FEDERAL FUNDS

SEC. 2. Section 303 of the Small Business Investment Act of 1958, as amended (15 U.S.C. 683), is amended by adding at the end thereof two new subsections as follows:

“(c) The Administration’s share of any loan made under subsection (b) to any small business investment company, after the effective date of this subsection, shall become immediately due and payable whenever the Administration determines that such company has suffered an impairment of capital (as defined in regulations prescribed by the Administration), and gives written notice to such company of such determination.

“(d) In furnishing financial assistance to any small business investment company under this section or section 302, after the effective date of this subsection, the Administration shall require such company to place in escrow, within a reasonable period of time (as determined by the Administration), securities or other obligations acquired by such company in the course of its business operations having an aggregate value which is not less at any time than the amount of outstanding loans and purchases made by the Administration in furnishing such assistance to such company. Securities or other obligations of any such company which are held in escrow under this section may be serviced, managed, and disposed of by such company subject to the above stated requirement with respect to the aggregate value of the securities or other obligations so held. Income or other receipts from securities or other obligations of any such company which are so held shall not, unless otherwise ordered pursuant to section 309(b), be placed in escrow but shall be fully available to such company in the conduct of its business operations. In the event of liquidation of any such company, or if a trustee or receiver is appointed for such company, securities or other obligations held in escrow pursuant to this section shall be treated as any other assets of such company.”

ADMINISTRATION, FIDELITY BONDS, CHANGES IN CONTROL, EXAMINATIONS

SEC. 3. Section 308(c) of the Small Business Investment Act of 1958, as amended (15 U.S.C. 687(c)), is amended to read as follows:

"(c) (1) The Administration shall prescribe regulations governing the operations of small business investment companies licensed under this Act, and to carry out the provisions of this Act in accordance with the purposes thereof. Such regulations shall include a requirement that each such company shall obtain and maintain a fidelity bond executed by a surety holding a certificate of authority from the Secretary of the Treasury, pursuant to the Act of August 13, 1894 (6 U.S.C., Secs. 6-13), as an acceptable surety on Federal bonds. Each officer, director, or employee of such company who has control over or access to cash securities or other property of the company shall be covered by such a bond. Any such bond shall conform to regulations prescribed by the Administration and shall be in an amount not less than the amount of outstanding loans and purchases made by the Administration in providing financial assistance to such company under sections 302 and 303. Such regulations shall also require each such company to report promptly to the Administration whenever a change occurs in the control of such company. As used herein, the term 'control' means the power through the ownership of stock or otherwise to change the management or policies of a small business investment company.

"(2) Small business investment companies licensed under this Act shall be subject to examination by examiners selected or approved by the Administration. Each such company shall receive such an examination at such times, not less often than once each year, as the Administration shall determine to be necessary or desirable: *Provided*, That each such company shall be examined not later than three months after it has been licensed under this Act, and not later than three months after the Administration has been notified that any change has occurred in the control of such company. Any such examination shall include an evaluation and classification with respect to the degree of risk and probability of loss involved in outstanding loans and investments made by any such company. The cost of such examinations, including the compensation of the examiners, may in the discretion of the Administration be assessed against the company examined, and when so assessed shall be paid by such company. Each such company shall make such reports to the Administration, at such times and in such form, as the Administration may require; except that the Administration may exempt from making such reports any company which is registered under the Investment Company Act of 1940 to the extent necessary to avoid duplication in reporting requirements."

ANNUAL REPORT TO THE CONGRESS

SEC. 4. Section 308 of the Small Business Investment Act of 1958, as amended (15 U.S.C. 687), is amended by adding at the end thereof a new subsection as follows:

"(f) The Administration shall include in its annual report to the Congress a full and detailed account of its operations under this Act. Such report shall set forth the amount of losses sustained by the Government as a result of such operations during the preceding fiscal year, together with an estimate of the total losses which the Government can reasonably expect to incur as a result of such operations.

CEASE AND DESIST ORDERS: ESCROW REQUIREMENT

SEC. 5. Section 309(b) of the Small Business Investment Act of 1958, as amended (15 U.S.C. 687a. (b)), is amended by inserting after the first sentence the following: "Such orders may, whenever the Administration deems it appropriate in order to conserve the assets of such licensee, require that income or other receipts derived from securities or other obligations of such licensee which are held in escrow pursuant to section 303(d) also be placed in escrow until otherwise directed by the Administration."

SBA AS TRUSTEE OR RECEIVER

SEC. 6. Section 311 of the Small Business Investment Act of 1958, as amended (15 U.S.C. 685c.), is amended by adding at the end thereof a new subsection as follows:

"(c) The Administration shall have authority to act as trustee or receiver of the licensee. Upon request by the Administration, the court may appoint the Administration to act in such capacity unless the court deems such appointment inequitable or otherwise inappropriate by reason of the special circumstances involved."

SELF-DEALING TRANSACTIONS AND CONFLICTS OF INTEREST

SEC. 7. Section 312 of the Small Business Investment Act of 1958, as amended (15 U.S.C. 687d), is amended—

- (1) by inserting "(a)" after "Sec. 312.";
- (2) by inserting "(A)" after "include" in the last sentence;
- (3) by striking out the period at the end of the last sentence and inserting in lieu thereof the following: ", and (B) an effective prohibition against any small business investment company purchasing equity securities of, or making any loan to, a small business concern, without prior written approval of the Administration, if any person affiliated with such company is also affiliated with such concern. As used herein, a person shall be deemed to be affiliated with a business enterprise if (i) he is an officer or director of, or partner in, such enterprise, or (ii) he directly or indirectly owns, controls, or holds with power to vote, 10 per centum or more of the outstanding voting shares of such enterprise: *Provided*, That nothing contained herein shall be construed to prohibit a licensee from permitting an officer, employee, or representative from serving as an officer, director, 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."; and

(4) by adding at the end thereof a new subsection as follows:

"(b) Any officer or director of a small business investment company licensed under this Act who knowingly participates in a violation of any regulation issued pursuant to clause (B) of the last sentence of subsection (a) of this section shall be fined not more than \$10,000 or imprisoned not more than one year, or both."

SBIC STOCK COLLATERAL FOR LOANS

SEC. 8. (a) Chapter 17 of Title 18, United States Code, is amended by adding at the end thereof a new section as follows:

"§ 338. Stock of small business investment companies as collateral for loans

"Whoever knowingly offers or receives shares of stock in any small business investment company, licensed under the provisions of the Small Business Investment Act of 1958, as security for any loan to purchase an interest in such company, or any other company so licensed, shall be fined not more than \$10,000 or imprisoned not more than one year, or both.

"This section shall not be construed to apply to any loan made prior to the effective date of this section, unless, after the expiration of thirty days after such date, such loan is secured in whole or in part by collateral consisting of shares of stock in any such company."

(b) The analysis to chapter 17 of Title 18, United States Code, is amended by adding at the end thereof a new item as follows:

"338. Stock of small business investment companies as collateral for loans."

Senator HARRIS. In addition to that, I have with me a memorandum prepared by John Brick of our subcommittee staff, which gives a side-by-side comparison of the legislation you have just inserted in the record, the proposed legislation and S. 3695, showing that actually

there is very little overlapping between the provisions of these two bills.

Senator PROXMIRE. Let me insert that in the record also at this point.

(The memorandum and attachment follow:)

MEMORANDUM

AUGUST 11, 1966.

To: Jerome S. Adlerman.

From: John Brick.

Subject: Proposed legislation on small business investment companies: Side-by-side comparison of bills.

Basically, the bill proposed by Senator Proxmire and the bill we have drafted for introduction by Senator McClellan have little in common. Senator Proxmire's bill generally seeks to improve and establish administrative and supervisory functions of the Small Business Administration in order to prevent the occurrence or recurrence of problems that have plagued the industry. The Subcommittee's bill seeks generally to accomplish the same objective, but it goes much farther in seeking to correct the conditions disclosed in our hearings and to curb their recurrence; additionally and most importantly, it seeks to provide for the recovery by the Federal Government of funds which have been lost already or may be lost in the future, and it seeks to safeguard the loans and investments made by the Small Business Administration in the SBIC program.

Since few of the provisions of the Subcommittee's bill have counterparts in Senator Proxmire's bill, the following side-by-side comparison will serve principally to point out the degree in which the Subcommittee's bill is more comprehensive and far-reaching. The comparison is attached to this memorandum.

SIDE-BY-SIDE COMPARISON OF PROPOSED SBIC LEGISLATION

SUBCOMMITTEE'S BILL

1. Sets limitation of 23½ percent on borrowing of private capital in a Small Business Investment Company.
2. Makes any Federal loan to an SBIC due and payable when such company suffers impairment of capital.
3. Requires an SBIC to place in escrow amounts equal to its Federal loans and investments.
4. Directs that the Small Business Administration prescribe regulations for SBIC's and for their administration.
5. Provides that each SBIC shall furnish fidelity bonds to cover Federal funds for performance of officers, directors, and employees.
6. Requires each SBIC to report promptly to SBA any change in control of the company.
7. Provides for annual examination of each SBIC, and further provides examinations within three months of licensing of a new company or of a company which has undergone change of control. Costs to be borne by SBIC's.
8. Requires the filing of all reports as may be directed by SBA.
9. Requires the filing of a detailed annual report, including losses and expected losses, to the Congress.
10. Subcommittee's bill provides that additional funds, from income of security placed in escrow may also be placed in escrow.
11. Provides that the Small Business Administration may act as trustee or receiver of an SBIC under court appointment.
12. Prohibits self-dealing transactions, for which violators are liable to \$10,000 fine, one year in prison, or both.
13. Prohibits the use of any SBIC stock as collateral for a loan to purchase stock in that SBIC or any other SBIC. Penalty for violation: \$10,000; one year in prison, or both.
14. Subcommittee's bill makes no similar provision.

SENATOR PROXMIRE'S BILL

1. No similar provision in Senator Proxmire's bill.
2. No similar provision in Senator Proxmire's bill.
3. No similar provision in Senator Proxmire's bill.
4. Makes similar specific provisions that the Administrator and the Small Business Administration shall have similar authority.
5. No similar provision in Senator Proxmire's bill.
6. No similar provision in Senator Proxmire's bill.
7. Makes companies subject to examination by direction of SBA, and the cost may be assessed against the company.
8. Requires the filing of all reports as may be directed by SBA.
9. No similar provision in Senator Proxmire's bill.
10. Senator Proxmire's bill makes no such provision.
11. Makes similar specific provisions for SBA to act as trustee or receiver.
12. Senator Proxmire's bill makes no such provision.
13. Senator Proxmire's bill makes no such provision.
14. Provides that SBA may revoke or suspend any SBIC license for false statements to SBA or for willfully violating or failing to observe either statute or regulations, or for violation of a cease and desist order by SBA.

15. Subcommittee's bill makes no similar provisions.
16. Subcommittee's bill makes no such provision.
17. Subcommittee's bill has several specific provisions against such actions, although none in this broad general language.
18. No such provision in Subcommittee's bill.
19. No similar provision in Subcommittee's bill.
20. Requires, as noted above, escrow and fidelity bond provisions, which are specific.
21. No similar provision.
22. No similar provision.
15. Authorizes SBA to issue cease-and-desist orders against persons or SBIC. May direct removal of officers or employees and prohibit further participation of such persons.
16. Violations by SBIC's shall be deemed to be also violations on part of persons who participate.
17. Makes unlawful any act in breach of fiduciary duty, if such act causes loss or other damage to SBIC.
18. Prohibits persons convicted of felonies or of fraud from serving in SBIC's.
19. Provides penalty of \$100 per day for failure to file any reports required.
20. Makes personally liable for all Federal indebtedness any person who knowingly participates in violations relating to Federal funds in SBIC's.
21. Provides for personal jurisdiction on actions on violations in district where SBIC maintains its principal office.
22. Reduces number of Deputy Administrators from 4 to 1. Provides for appointment of three Associate Administrators.

Senator HARRIS. I have a summary, Mr. Chairman, of the legislation which I have just referred to and I would like to offer that also at this time.

Senator PROXMIRE. Without objection, it will be inserted in the record.

(The summary follows:)

SUMMARY OF A BILL TO STRENGTHEN CERTAIN PROVISIONS OF LAW RELATING TO THE ORGANIZATION, OPERATION AND SUPERVISION OF SMALL BUSINESS INVESTMENT COMPANIES

Section 1. Limitation on borrowed private capital for small business investment companies

This section of the bill amends Section 302(a) of the Small Business Investment Act of 1958, as amended, by limiting the amount of borrowed funds that may be utilized as private capital in a Small Business Investment Company to 33 $\frac{1}{2}$ percent of the company's paid-in capital and surplus, excepting that the limitation does not apply to companies licensed as Small Business Investment Companies prior to the date of enactment of this act.

Section 2. Safeguarding of Government funds

Two new subsections are added to the existing statute to provide:

1. That any Federal loan to a Small Business Investment Company becomes due and payable whenever such company suffers an impairment of capital as determined by Small Business Administration regulations.

2. That a Small Business Investment Company is required to place adequate security in escrow in amounts at least equal to its Federal loans or investments.

Section 3. Administration; fidelity bonds; changes in company control; examination

This section provides:

Administration.—The Small Business Administration shall prescribe regulations for the operations of SBIC's and for the administration of the SBIC program.

Fidelity Bonds.—Each SBIC shall furnish a surety bond in an amount equal to the financial aid furnished by the Government, which will bind performance by officers, directors and employees of each such SBIC.

Changes in Control. Each SBIC shall report promptly to the SBA any change of control of the company.

Examinations.—Each SBIC shall be examined by SBA at least once a year. Examinations will be made within three months after licensing, and within three months after changes in control. Such examinations will evaluate risks and probabilities of losses, and the costs of examination may be borne by the SBIC at the discretion of the SBA. Each SBIC will file reports as required by the SBA.

Section 4. SBA report to the Congress

The Small Business Administration is required to file a detailed report annually to the Congress relating to SBIC operations, including the amount of losses to the Government for the preceding fiscal year and a reasonable estimate of losses expected during the current fiscal year.

Section 5. Additional escrow provision

This section provides that, in the discretion of SBA, the income or other receipts from the "adequate security" placed in escrow as required in Section 2 of this bill may also be placed in escrow.

Section 6. The SBA as trustee or receiver

The Small Business Administration is authorized to act as trustee or receiver of a licensed company, under court appointment.

Section 7. Self-dealing transactions

SBIC's are prohibited from investing in or lending to small business concerns whenever any person affiliated with the SBIC is affiliated with the small business concern. Affiliation is deemed to be ownership or control of 10 percent of a business enterprise. This section provides that violators may be liable to \$10,000 fine, two years in prison, or both.

Section 8. Use of SBIC stock as collateral

This section provides that no person may offer or receive stock of any SBIC as security for a loan to purchase an interest in that company or any other SBIC. Penalty for violation may be a fine of \$10,000, or one year in prison, or both.

Senator HARRIS. At the close of our hearings on small business investment companies, I issued a statement I would like to present briefly. It says this:

We have now come to the conclusion of three days of testimony concerning Small Business Investment Companies and their regulation by the Small Business Administration. First of all, I want to thank all of the witnesses for their patience in sitting through some long sessions so that we could finish on schedule.

I want to commend particularly Mr. Bernard Boutin, Administrator of the Small Business Administration, and the Deputy Administrator, Mr. Howard Greenberg, for their candid and forthright testimony. It was indeed reassuring and refreshing to listen to a straightforward admission on their part of the existence of severe problems in this program and a factual discussion by them of means being employed to solve them. The fact that these problems are out in the open is a major step forward in getting them under control.

And I reemphasize here, Mr. Chairman, how impressed I was and our subcommittee was by Mr. Boutin and Mr. Greenberg, their attitude and the efforts that they have undertaken to see that this program functions in accordance with the intent of Congress.

I then said:

Once again, I feel sure I am joined by the other members of the Subcommittee in expressing our confidence that Mr. Boutin and his formidable administrative talents will get this program back on the track and doing the job Congress intended that it should do.

I then said also:

To maintain proper perspective, we have placed in the record testimony concerning the many fine people who are associated with SBIC's and the good records that they have made in carrying out the intent of Congress.

But it has been a shocking thing to learn that a program with so many taxpayers' dollars involved could exist for so long in such a lax condition of federal administration.

It was distressing to learn of the failure by SBA to check out the people who were going to receive U.S. money; to learn that companies with Government funds could go as long as four years without examination; to learn that the accounting system of SBA had broken down; to learn that nobody knows and will not know till later how much money the Government may lose in this program; to learn that little has been done to salvage the assets of companies in trouble.

It was shocking to find such a small effort had been made by SBA to weed out the cheats, the swindlers and the incompetents from the program.

And our records were replete with evidence which substantiated that statement.

It is a sad commentary that the SBA which has the responsibility through this program to stimulate, encourage and nourish small business has set such a sorry example in its own lax and inefficient business practices in regard to Small Business Investment companies.

The individual companies we have examined have also produced some ugly realities. In one case on which we heard testimony there was a blatant piracy of a corporation financed with federal funds by men who had no money of their own at risk at all.

The other cases were almost as bad, and they showed the same pattern: "bootstrapping" the operation with somebody else's money; self-serving loans to companies owned and controlled by the same individuals; the use of corporate money (including Government money) for personal purposes and finally and

unfortunately an apathy and lethargy on the part of SBA which allowed these situations to exist for an intolerably long period.

In one of the cases, based on information from the Subcommittee staff, the SBA did move and as a result \$400,000 was retrieved for the Government. In the other two, it appears that there will be losses of 100 percent, or a total of almost a million and a half dollars loss by the Government in those two companies alone.

We certainly don't want to rock the boat while Mr. Boutin is going ahead full steam with his corrective program. But Congress does have a real interest here and I am going to ask our staff to continue inquiries into other problem areas which we have not discussed in depth here. It is entirely possible that after the crash examination program is completed by SBA and an estimate of losses on a realistic basis is available, we may ask Mr. Boutin to come back and report to us on these subjects. In the meantime, I know we can count on the continued splendid cooperation we have received from Mr. Boutin and his staff.

And I might say further, as a result of our hearings and the evidence which was brought out there by the action of our subcommittee, I furnished complete copies of our hearings to the Justice Department and to others for whatever criminal action or other action might be necessary and also whatever action might be necessary to protect the Government's interests in some of these companies which are in trouble.

I think that S. 3695 is a bill which ought to be passed either in its present form or as might be decided upon by this subcommittee to make it more workable. It provides that persons convicted of felonies may not serve in SBIC's. It give the Administration the power to revoke as well as to suspend licenses for cause and this, I think, is a fuzzy area of the law right now—what can be done and upon what grounds?

It gives the SBA power to issue cease and desist orders against individuals for cause and to direct the removal of officers, directors, or other employees who have wilfully violated the act or regulations. It clarifies the status of the investment program within the Small Business Administration. It provides for the personal liability of officers and directors where their wilful violation of the act or regulations has caused a loss to the SBA or to the SBIC.

This latter provision is one, I know, that gives much concern to those involved in this industry and perhaps could be softened or made more workable so that you would not hinder the bringing of good people into this program and not hinder good people continuing to serve on board for fear that they might become personally liable for acts of the corporation when it was not a wilful and intentional violation of the act or regulation.

I think these are things which can be worked out by this subcommittee, but I think the basic ideas of this act are needed and Mr. Boutin has testified before our committee and this one, I'm sure, is needed. It provides for examinations not only of the SBIC itself, but also of the companies which receive loans or investments from the SBIC, which companies are in many cases, the actual ultimate recipient of the Government's money.

So, I think what we need to do here is to give some additional tools to SBA to do the job that I'm confident they want to do. Nobody in the Congress of the United States feels more strongly about the place of small business in this country than do I. And I want to commend as heartily as I know how the excellent and fruitful efforts that you have made, Mr. Chairman, over the years, in programs designed by the Congress to foster the growth and development of small business in this country.

I think that the SBIC program is one which was well conceived in principle. It had wide, almost unanimous approval of the Members of the Congress when it was initiated in 1958. The spirit of that law is still good, but I think we have been entirely too lax and I think the Congress is to blame, as well as the SBA, in not giving some more assistance and guidelines on administration and operation of these companies to the vast majority of people who got into this business with a sincere desire to operate well and within the spirit as well as the letter of the regulations and the law, which is, I think, the situation in this industry.

We were lax, I think, also in not trying to search out and eliminate those people, and there were a good many, who came into this program with not such a sincere desire to operate within the spirit and letter of this law and of the regulations of SBA. But if this program is a good program, as I believe it is, and if it is to be continued, if the Congress of the United States is to continue to put money into this program, it seems to me that we have a special responsibility in view of some of the things that have come out in these hearings to see that we have helped SBA clean its house, as Mr. Boutin and Mr. Greenberg have testified they want to do and as representatives of the SBIC's themselves have testified that they want to do.

I have talked with a good many of those people. I think there are things that we need to do legislatively and I know the chairman thinks so also, which might give better incentive to people in these businesses and better incentive for their effective operation. But, I think before we talk about changes in the law of that type, we need to make changes in the laws concerning the operation and administration of this program to assure the Congress and to assure the taxpayers that we are operating as well as we possibly could with their money.

So I commend the chairman. I won't go into the details of the bill which our staff has prepared, but I hope it will be taken into consideration along with S. 3695, and that changes will be made as you, Mr. Chairman, and this subcommittee decide, are necessary in your judgment and wisdom to make the program do what we want it to do and to make S. 3695 and this bill do what we want it to do, but at the same time eliminate any unnecessarily harsh effect on this industry.

Senator PROXMIRE. I want to thank you very, very much, Senator Harris. I know you have another committee meeting and I have to go to the floor myself, but I would like to say not only what you have given us this morning is most helpful, but the investigation that you made certainly has had a great deal to do, I think, with the kind of forceful legislation and administration you indicate we need.

What I would like to suggest, because this is late in the session and we are anxious to get action on S. 3695 in some form, is that you have Mr. Walsh meet at his convenience with Mr. Barnes and Mr. Egenroad. Mr. Barnes, you know, is our chief staff man on small business. Mr. Egenroad is minority chief staff man. If they can meet today or tomorrow, because it is very urgent we get action on this so we can have a markup session on this bill just as soon as we can, that would be appreciated.

Senator HARRIS. Mr. Walsh is here, Mr. Chairman, and we will certainly do that.

Senator PROXMIRE. I have talked to Mr. Barnes and I'm sure Mr. Egenroad will also do his best to accommodate you so those three men can get together to see what they can do about working the provisions of your bill, some of them, into S. 3695.

I think that we found out yesterday that S. 3695 is far more controversial than we originally anticipated and because this is late in the session, I think we know we can't get a very controversial bill through both Houses and get it enacted into law, so we are going to have to cut down on S. 3695 to some extent at least.

I think the same thing may apply to your bill. This doesn't mean that we won't try again perhaps next year on some of these measures, but I think that certainly for this year, we will have to do what we can to get a bill that is pretty much agreed upon.

I think everybody wants to eliminate the crooked operators and sharp operators and have a good, clean, crisp program, but as was said by one very effective witness yesterday, we don't want the cleanest but emptiest program in the Government. We want a program that really does the job for small business that we all know has to be done.

Senator HARRIS. I certainly agree, Mr. Chairman, with what you have said and we will be very happy to accept your suggestions. Mr. Walsh will work with your committee staff and see what we can work out because, as you say, we certainly don't have time to go into perhaps all of the provisions of both of these bills and work them out as we might like to.

I think it really would be a shame if we came back here next year and said to Mr. Boutin, "Well, what have you been doing about some of these things?" and he said, "Well, as I told you last year, I just don't have the tools that I need to work with."

I think it is imperative that where we have an Administrator, such as he, who wants to do something, who wants these additional tools, that we give him as much as we can without hurting the industry.

We don't want to do that and we don't want to damage the great majority of these people who are doing a good job and perhaps we can do, as you say, take some of these things that are maybe not so hard to work out and are not quite so controversial and give Mr. Boutin the basic tools he needs to do this. I really join with you in the hope that can be done.

Senator PROXMIRE. Thank you very, very much, Senator.
(The prepared statement of Senator Harris follows:)

PREPARED STATEMENT OF FRED R. HARRIS, U.S. SENATOR FROM THE STATE OF OKLAHOMA

Mr. Chairman and members of the Subcommittee, I am most happy to have the opportunity to appear before you to testify in support of S. 3695 and also S. — which are bills designed to strengthen our laws concerning the Small Business Investment program.

There was a remarkable unanimity among all the members of the Senate on the value of this program when it was initiated in 1958. Its purpose was certainly a worthwhile one; to help small business in an area where small business is particularly in distress. This is the availability or lack of availability of sources for long-term financing.

Everyone was in agreement that it was a proper thing for the Federal Government to foster and stimulate an industry composed of privately-owned com-

panies which would make available long-term loans and equity capital to small business concerns; further, it was proper to loan U.S. funds to the individual companies in this fledgling industry to help them get started. And so, the program began with a bright hope to perform a badly needed function in our present day business framework.

But this program like all other programs is made up of human beings doing business with other human beings and, therefore, the opportunity exists for all the failures and shortcomings which men are capable of.

In 1965, the Senate Permanent Subcommittee on Investigations of the Government Operations Committee was engaged in a prolonged investigation of certain abuses and excesses by financial racketeers in the banking industry.

Disquieting information was received that these predators had sensed an opportunity to move into the Small Business Investment program and use it, not to help build small business in a worthwhile way, but to drain out money to line their own pockets for their own personal advantage.

The Investigations Subcommittee did look into these allegations. As you are aware, the hearings recently held by this Subcommittee itself, by the House Committee on Small Business, and by the Investigations Subcommittee showed that these allegations were unfortunately only too true.

The combination of the greed and rapacity of certain unscrupulous financial operators with a weak and ineffective administration of the program did allow serious inroads to be made which diverted Government money from the intended purposes of the Congress and which may very well result in some heavy losses to the U.S. Government.

In the hearings, we had the opportunity to hear Mr. Bernard Boutin, the new Administrator of the Small Business Administration, and his deputy, Mr. Howard Greenberg. Their approach to the major task of clean up which faces them was certainly reassuring; however, they stressed the fact that they need certain legal tools to use in this task.

It is our duty and responsibility to see that they get these tools and that is why I repeat that I am happy to be here today to testify in favor of this legislation.

S-3695 was introduced by the distinguished Senator from Wisconsin, the Chairman of this Subcommittee, and I had the pleasure to serve as co-sponsor for the bill along with the distinguished Senators from Alabama, Texas, and South Dakota, Senator Sparkman, Senator Tower, and Senator Mundt.

The provisions of this bill were largely the recommendations of the Small Business Administration to clarify and strengthen the powers available to them under the Act to administer and supervise the individual Small Business Investment companies receiving licenses and Federal funds from the Administration.

It provides that persons convicted of felonies may not serve in SBIC's; it gives the Administration the power to revoke as well as to suspend licenses for cause; it gives the Administration the power to issue cease and desist orders against individuals for cause and to direct the removal of officers, directors, or other employees who have willfully violated the Act or Regulations. It clarifies the status of the Investment Program within the Small Business Administration. It provides for the personal liability of officers and directors where their willful violation of the Act or Regulations has caused a loss to the SBA or to the SBIC.

It provides for examinations not only of the SBIC but also of the companies which receive loans or investments from the SBIC which companies are in many cases the actual ultimate recipients of Government money.

Mr. Chairman, the hearings before the Permanent Subcommittee on Investigations in which I had the honor to serve as Acting Chairman indicated to me very forcefully the necessity for this legislation which will help the Administration in their campaign to clean up the Investment program and that is why I want to endorse this bill wholeheartedly and without reservation.

But there are some other problems which were brought out in the hearings before the Permanent Subcommittee on Investigations and that is why I want to urge your serious consideration of S. —.

First of all, both in the present situation and in the banking investigation, we found that one of the consistent characteristics of the financial looters of these institutions was that they had no funds of their own at risk in the enterprise. They operated almost exclusively with borrowed money and the risk in these companies fell then on the Government, the banks, savings and loan associations, etc., who loaned them the money.

That is why we have included in S. — a provision which requires that at least two-thirds of the capital investment in an SBIC must be the personal funds of the stockholders, not money borrowed from a bank or otherwise secured by the stock of the SBIC pledged as collateral. The purpose is to assure that the stockholders of the SBIC are actually sharing in the risk of the operation with the Government.

It was brought out in the hearing that there is a question within SBA as to whether there is legal authority for SBA to determine when a company has suffered losses to the extent that it is capitally impaired. A provision was written to make this authority unequivocal and to give the SBA the power to call the loan of a company which is capitally impaired under the definition.

Since a major problem brought out in the hearings was that because of the delays encountered in initiating legal action to retrieve the Government loans to SBIC's, it was found in unfortunately too many cases that by the time the Government was able to act, there were no assets left to levy upon.

A provision has, therefore, been written to require that when an SBIC receives Government money, an escrow account be maintained with loans and investments of the SBIC contained therein equalling the amount of the Government advance. The account was to be maintained in such a way that the SBIC was not hampered in its day-to-day normal operations. However, if the company became capitally impaired or involved in a violation of the Act or Regulations, the Government could call the loan and immediately tie up assets of the SBIC equal to the Government loan until legal action to appoint a receiver or conservator had taken place. The Government's position as a general or subordinate creditor would not be changed by this proceeding.

It was brought out in the hearings that willful violations of the conflict of interest provisions do not at present carry any criminal penalties. Such penalties were provided. Other provisions include a requirement for surety bond coverage to equal the Government loans, for a detailed report to Congress annually including an estimate of losses to be incurred, for an annual examination of each SBIC, and for examination immediately on changes in ownership.

Mr. Chairman, the provisions in both of these bills were not intended to harass or interfere with the operators of legitimate SBIC's. They are aimed at helping the Administration expel the undeserving and the undesirables from the program.

I believe that if we want to keep this program alive and obtain the benefits from it which we expected in the beginning, then this legislation is urgently needed and I strongly recommend the serious consideration and immediate passage of all of the provisions set out in both bills.

Senator PROXMIRE. This concludes the testimony on S. 3695. The committee will stand adjourned.

(Whereupon, at 10:20 a.m., the committee was adjourned.)

[Excerpts from U.S. Code, Title 18]

§ 212. Offer of loan or gratuity to bank examiner.

Whoever, being an officer, director or employee of a bank which is a member of the Federal Reserve System or the deposits of which are insured by the Federal Deposit Insurance Corporation, or of any National Agricultural Credit Corporation, or of any land bank, Federal land bank association or other institution subject to examination by a farm credit examiner, or of any small business investment company, makes or grants any loan or gratuity, to any examiner or assistant examiner who examines or has authority to examine such bank, corporation, or institution, shall be fined not more than \$5,000 or imprisoned not more than one year, or both; and may be fined a further sum equal to the money so loaned or gratuity given.

The provisions of this section and section 218 of this title shall apply to all public examiners and assistant examiners who examine member banks of the Federal Reserve System or insured banks, or National Agricultural Credit Corporations, whether appointed by the Comptroller of the Currency, by the Board of Governors of the Federal Reserve System, by a Federal Reserve Agent, by a Federal Reserve bank or by the Federal Deposit Insurance Corporation, or appointed or elected under the laws of any state; but shall not apply to private examiners or assistant examiners employed only by a clearinghouse association or by the directors of a bank. (June 25, 1948, ch. 645, § 212, formerly § 217, 62 Stat. 694, amended Aug. 21, 1958, Pub. L. 85-699, title VII, § 701(a), 72 Stat. 698; Aug. 18, 1959, Pub. L. 86-168, title I, § 104(h), 73 Stat. 387; renumbered Oct. 23, 1962, Pub. L. 87-849, § 1(d), 76 Stat. 1125.)

LEGISLATIVE HISTORY

Reviser's Note.—Based on sections 593 and 1245 of title 12, U.S.C., 1940 ed., Banks and Banking (Dec. 23, 1913, ch. 6, § 22, 38 Stat. 272; Sept. 26, 1918, ch. 177, § 5, 40 Stat. 970; Mar. 4, 1923, ch. 252, title II, § 209 (e), 42 Stat. 1468; Feb. 25, 1927, ch. 191, § 15, 44 Stat. 1232; Aug. 23, 1935, ch. 614, § 326(a), 49 Stat. 715).

Section 593 of title 12, U.S.C., 1940 ed., Banks and Banking, was divided into three sections: this section and sections 218 and 655 of this title.

Words "shall be deemed guilty of a misdemeanor and" were omitted as unnecessary in view of definition of misdemeanor in section 1 of this title.

This section was expanded to include "National Agricultural Credit Corporations" by including this term in each paragraph, upon authority of section 1245 of title 12, U.S.C., 1940 ed., Banks and Banking.

No penalty was provided for offering a bribe to farm credit examiners. The words "or of any land bank, national farm loan association, or other institution subject to examination by a farm credit examiner," were added upon the authority of section 952 of said title 12.

Reference to persons causing or procuring was omitted as unnecessary in view of definition of "principal" in section 2 of this title.

Changes in phraseology were also made.

REFERENCES IN TEXT

Section 218 of this title, referred to in the text, is a reference to section 218 prior to its redesignation as section 213 of this title by section 1(d) of Pub. L. 87-849.

PRIOR PROVISIONS

A prior section 212, act June 25, 1948, ch. 645, 62 Stat. 693, which related to an offer or threat to a customs officer or employee, was eliminated in the general amendment to this chapter by Pub. L. 87-849 and is substantially covered by revised section 201.

AMENDMENTS

1959—Pub. L. 86-168 substituted "Federal land bank association" for "national farm loan association".

1958—Pub. L. 85-699 included officers, directors and employees of small business investment companies.

EFFECTIVE DATE OF 1959 AMENDMENT

Amendment of section by Pub. L. 86-168 effective Dec. 31, 1959, see section 104(k) of Pub. L. 86-168, set out as a note under section 751 of Title 12, Banks and Banking.

EXCEPTION AS TO TRANSFER OF FUNCTIONS

Functions vested by any provision of law in the Comptroller of the Currency, referred to in this section, were not included in the transfer of functions of officers, agencies and employees of the Department of the Treasury to the Secretary of the Treasury, made by 1950 Reorg. Plan No. 26, § 1, eff. July 31, 1950, 15 F.R. 4935, 64 Stat. 1280, set out in note under section 241 of Title 5, Executive Departments and Government Officers and Employees.

* * * * *

§ 213. Acceptance of loan or gratuity by bank examiner.

Whoever, being an examiner or assistant examiner of member banks of the Federal Reserve System or banks the deposits of which are insured by the Federal Deposit Insurance Corporation, or a farm credit examiner or examiner of National Agricultural Credit Corporations, or an examiner of small business investment companies, accepts a loan or gratuity from any bank, corporation, association or organization examined by him or from any person connected therewith, shall be fined not more than \$5,000 or imprisoned not more than one year, or both; and may be fined a further sum equal to the money so loaned or gratuity given, and shall be disqualified from holding office as such examiner. (June 25, 1948, ch. 645, § 213, formerly § 218, 62 Stat. 695, amended Aug. 21, 1958, Pub. L. 85-699, title VII, § 701(b), 72 Stat. 698; renumbered Oct. 23, 1962, Pub. L. 87-849, § 1(d), 76 Stat. 1125.)

LEGISLATIVE HISTORY

Reviser's Note.—Based on sections 593, 952, 981, 1124, 1243, 1314 of title 12, U.S.C., 1940 ed., Banks and Banking (Dec. 23, 1913, ch. 6, § 22, 38 Stat. 272; July 17, 1916, ch. 245, §§ 28, 31, 39 Stat. 381, 382, and § 211(d) as added Mar. 4, 1923, ch. 252, § 2, 42 Stat. 1460; Sept. 26, 1918, ch. 177, § 5, 40 Stat. 970; Mar. 4, 1923, ch. 252, title II, § 209(e), 216(d), 42 Stat. 1468, 1471; Feb. 25, 1927, ch. 191, § 15, 44 Stat. 1232; Ex. Ord. No. 6084, Mar. 27, 1933; June 16, 1933, ch. 98, § 80(a), 48 Stat. 273; Aug. 23, 1935, ch. 614, § 326(a), 49 Stat. 715; Aug. 19, 1937, ch. 704, § 20, 50 Stat. 710).

This section is derived primarily from second paragraph of section 593 of title 12, U.S.C., 1940 ed., Banks and Banking, and consolidates provisions from sections 952, 981, 1124, 1243, and 1314 of said title 12.

Words "shall be deemed guilty of a misdemeanor" were omitted in view of definition of misdemeanor in section 1 of this title.

The bribery provisions of such sections were alike and indeed were patterned after section 593 of said title 12, U.S.C., 1940 ed., Banks and Banking, incorporated in this section and section 217 of this title. Therefore, and in the light of sections 952 and 1243 of title 12, U.S.C., 1940 ed., Banks and Banking, this section and written as a consolidated section without change of substance or effect and with only such changes of phraseology as were necessary to effect the consolidation and secure uniformity of style.

Other provisions of said sections 593, 952, 981, 1124, 1243 and 1314 of title 12, U.S.C., 1940 ed., are incorporated in sections 217, 655, 1014, 1908, and 1909, of this title.

PRIOR PROVISIONS

A prior section 213, act June 25, 1948, ch. 645, 62 Stat. 693, which related to the acceptance or demand of a bribe by a customs officer or employee, was eliminated in the general amendment to this chapter by Pub. L. 87-849 and is substantially covered by revised section 201.

AMENDMENTS

1958—Pub. L. 85-699 included examiners of small business investment companies.

CROSS REFERENCES

Civil liability of officers or directors for violations, see section 503 of Title 12, Banks and Banking.

Offer of loan or gratuity to public examiners, see section 212 of this title.

Secret Service, arrest of violators, see section 3056 of this title.

* * * * *

§ 216. Receipt or charge of commissions or gifts for farm loan, land bank, or small business transactions.

Whoever, being an officer, director, attorney, or employee of a Federal land bank association, a Federal land bank, or a joint-stock land bank, organized or acting under authority of any law of the United States, or a small business investment company, is a beneficiary of or receives, directly or indirectly, any fee, commission, gift, or other consideration for or in connection with any transaction or business of such association or bank, other than the usual salary or director's fee paid to such officer, director, or employee thereof, and a reasonable fee paid by such association or bank to such officer, director, attorney, or employee for services rendered, shall be fined not more than \$5,000 or imprisoned not more than one year, or both.

Whoever causes or procures any Federal land bank, joint-stock land bank or Federal land bank association, organized under any Act of Congress, or any small business investment company, to charge or receive any fee, commission, bonus, gift, or other consideration not specifically authorized, shall be fined not more than \$5,000 or imprisoned not more than one year, or both. (June 25, 1948, ch. 645, § 216, formerly § 221, 62 Stat. 695, amended Aug. 21, 1958, Pub. L. 85-699, title VII, § 702(a)—(c), 72 Stat. 698; Aug. 18, 1959, Pub. L. 86-168, title I, § 104(h), 73 Stat. 387; renumbered Oct. 23, 1962, Pub. L. 87-849, § 1(d), 76 Stat. 1125.)

LEGISLATIVE HISTORY

Reviser's Note.—Based on section 983 of title 12, U.S.C., 1940 ed., Banks and Banking (July 17, 1916, ch. 245, § 31, 39 Stat. 382).

Section was formed from the first, second, and fourth sentences of said section 983 of title 12, U.S.C., 1940 ed., Banks and Banking. No change was made other than the usual verbal changes for style purposes, and some transposition of phrases incident to separation and consolidation of these particular sentences.

Word "organized or acting under authority of any law of the United States" were substituted for "organized under this chapter" because of the transfer.

The third sentence of said section 983 of title 12, U.S.C., 1940 ed., Banks and Banking, relating to disclosure of information by examiners, was separated and transferred to the chapter "Public Officers and Employees" in this title, where it was consolidated with similar provisions taken from section 1124 of title 12, U.S.C., 1940 ed., Banks and Banking, to constitute section 1907 of this title, the punishment provisions of both sections, insofar as relating to such disclosure, being identical.

AMENDMENTS

1959—Pub. L. 86-168 substituted "Federal land bank association" for "national farm loan association" wherever appearing.

1958—Pub. L. 85-699 included small business transactions in the catchline, officers, directors, attorneys and employees of small business investment companies in the first paragraph, and small business investment companies in the second paragraph.

EFFECTIVE DATE OF 1959 AMENDMENT

Amendment of section by Pub. L. 86-168 effective Dec. 31, 1959, see section 104(k) of Pub. L. 86-168, set out as a note under section 751 of Title 12, Banks and Banking.

REPEALS

A prior section 216, act June 25, 1948, ch. 645, 62 Stat. 694, which related to the procurement of a contract by an officer or Member of Congress, was repealed by section 1 (c) of Pub. L. 87-849.

CROSS REFERENCES

Secret service, detection, arrest, and delivery into custody of any person violating this section, see section 3056 of this title.

* * * * *

§ 657. Lending, credit and insurance institutions.

Whoever, being an officer, agent or employee of or connected in any capacity with the Reconstruction Finance Corporation, Federal Deposit Insurance Corporation, Home Owners' Loan Corporation, Farm Credit Administration, Federal Housing Administration, Federal Crop Insurance Corporation, Farmers' Home Corporation, the Secretary of Agriculture acting through the Farmers' Home Administration, or any land bank, intermediate credit bank, bank for cooperatives or any lending, mortgage, insurance, credit or savings and loan corporation or association authorized or acting under the laws of the United States or any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or any small business investment company, and whoever, being a receiver of any such institution, or agent or employee of the receiver, embezzles, abstracts, purloins or willfully misapplies any moneys, funds, credits, securities or other things of value belonging to such institution, or pledged or otherwise intrusted to its care, shall be fined not more than \$5,000 or imprisoned not more than five years, or both; but if the amount or value embezzled, abstracted, purloined or misapplied does not exceed \$100, he shall be fined not more than \$1,000 or imprisoned not more than one year, or both. (June 25, 1948, ch. 645, 62 Stat. 729; May 24, 1949, ch. 139, § 11, 63 Stat. 90; July 28, 1956, ch. 773, § 1, 70 Stat. 714; Aug. 21, 1958, Pub. L. 85-699, title VII, § 703, 72 Stat. 698; Oct. 4, 1961, Pub. L. 87-353, § 3(q), 75 Stat. 774.)

LEGISLATIVE HISTORY

Reviser's Note.—Based on sections 1026(b) and 1514(c) of title 7, U.S.C., 1940 ed., Agriculture, and sections 264(u), 984, 1121, 1138d(c), 1311, 1441(c), 1467(c), and 1731(c) of title 12, U.S.C., 1940 ed., Banks and Banking, and section 616(c) of title 15, U.S.C., 1940 ed., Commerce and Trade (Dec. 23, 1913, ch. 6, § 12B(u), as added June 16, 1933, ch. 89, § 8, 48 Stat. 178; July 17, 1916, ch. 245, § 31, fourth paragraph, 39 Stat. 382; July 17, 1916, ch. 245, § 211(a), as added Mar. 4, 1923, ch. 252, § 2, 42 Stat. 1459; Mar. 4, 1923, ch. 252, title II, § 216(a), 42 Stat. 1471; Jan. 22, 1932, ch. 8, § 16(c), 47 Stat. 11; July 22, 1932, ch. 522, § 21(c), 47 Stat. 738; Mar. 27, 1933, Ex. Ord. No. 6084; June 13, 1933, ch. 64, § 8(c), 48 Stat. 135; June 16, 1933, ch. 98, § 64(c), 48 Stat. 268; Jan. 31, 1934, ch. 7, § 13, 48 Stat. 347; June 27, 1934, ch. 847, § 512(c), 48 Stat. 1265; Aug. 23, 1935, ch. 614, § 101, 49 Stat. 701; July 22, 1937, ch. 517, title IV, § 52(b), 50 Stat. 532; Feb. 16, 1938, ch. 30 title V, § 514(c), 52 Stat. 76; Aug. 14, 1946, ch. 964, § 3, 60 Stat. 1064).

Each of the eleven sections from which this section was derived contained similar provisions relating to embezzlement, false entries, and fraudulent issuance or assignment of obligations with respect to one or more named agencies or corporations.

These were separated and the embezzlement and misapplication provisions of all form the basis of this section, and with one exception the remaining provisions of each section forming the basis for section 1006 of this title. The sole exception was that portion of said section 616(c) of title 15 as to the disclosure of information which now forms section 1904 of this title.

The revised section condenses and simplifies the constituent provisions without change of substance except as in this note indicated.

The punishment in each section was the same except that in section 1026(b) of title 7, U.S.C., 1940 ed., Agriculture, and sections 984, 1121, and 1311 of title 12, U.S.C., 1940 ed., Banks and Banking, the maximum fine was \$5,000. The revised section adopts the \$5,000 maximum. (For same penalty covering similar offense, see section 656 of this title.)

The smaller punishment for an offense involving \$100 or less was added. (See reviser's notes to section 641-645 of this title.)

The enumeration of "moneys, funds, credits, securities, or other things of value" does not occur in any one of the original sections but is an adequate, composite enumeration of the instruments mentioned in each.

References to persons aiding and abetting contained in sections 984, 1121, 1311 of title 12, U.S.C., 1940 ed., Banks and Banking, were omitted as unnecessary, such persons being made principals by section 2 of this title.

The term "receiver" is used in sections 1121 and 1311 of title 12, U.S.C., 1940 ed., Banks and Banking, with reference to Federal intermediate banks and agricultural credit corporations, and is undoubtedly embraced in the term "connected in any capacity with," but the phrase "and whoever, being a receiver of any such institution" was inserted in this section to obviate all doubt as to its comprehensive scope.

The suggestion has been made that "private examiners" should be included. These undoubtedly are covered by the words "connected in any capacity with." (See also section 655 of this title.)

The term "or any department or agency of the United States" was inserted in each revised section in order to clarify the sweeping provisions against fraudulent acts and to obviate any possibility of ambiguity by reason of the omission of specific agencies named in the constituent sections. (See section 6 of this title defining "department and agency." For other verbal changes and deletions see reviser's note under section 656 of this title.)

SENATE REVISION AMENDMENT

The text of this section was changed by Senate amendment. See Senate Report No. 1620, amendment No. 7, 80th Cong.

AMENDMENTS

1961—Pub. L. 87-353 struck out "Federal Farm Mortgage Corporation," following "Federal Housing Administration,".

1958—Pub. L. 85-699 included officers, agents or employees of or connected in any capacity with small business investment companies.

1956—Act July 28, 1956, included officers, agents or employees of or connected in any capacity with any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation.

1949—Act May 24, 1949, made section applicable to “the Secretary of Agriculture acting through the Farmers’ Home Administration.”

EXCEPTIONS FROM TRANSFER OF FUNCTIONS

Functions of the Corporations of the Department of Agriculture, the boards of directors and officers of such corporations; the Advisory Board of the Commodity Credit Corporation; and the Farm Credit Administration or any agency, officer or entity of, under, or subject to the supervision of the said Administration were excepted from the functions of officers, agencies and employees transferred to the Secretary of Agriculture by 1953 Reorg. Plan No. 2, § 1, eff. June 4, 1953, 18 F.R. 3219, 67 Stat. 633, set out as a note under section 511 of Title 5, Executive Departments and Government Officers and Employees.

ABOLITION OF HOME OWNERS’ LOAN CORPORATION

For dissolution and abolishment of Home Owners’ Loan Corporation, referred to this section, by act June 30, 1953, ch. 170, § 21, 67 Stat. 126, see note under section 1463 of Title 12, Banks and Banking.

FARM CREDIT ADMINISTRATION

Establishment of Farm Credit Administration as independent agency, and other changes in status, functions, etc., see section 636a et seq., of Title 12, Banks and Banking.

ABOLITION OF RECONSTRUCTION FINANCE CORPORATION

Section 6(a) of 1957 Reorg. Plan No. 1, eff. June 30, 1957, 22 F.R. 4633, 71 Stat. 647, set out as a note under section 601 of Title 15, Commerce and Trade, abolished the Reconstruction Finance Corporation.

CROSS REFERENCES

Financial control of government corporations, see chapter 14 of Title 31, Money and Finance.

Secret Service, detection, arrest and delivery into custody of any person violating this section in so far as the Federal Deposit Insurance Corporation, Federal land banks, joint-stock land banks and national farm loan associations are concerned, see action 3056 of this title.

* * * * *

§ 1006. Federal credit institution entries, reports and transactions.

Whoever, being an officer, agent or employee of or connected in any capacity with the Reconstruction Finance Corporation, Federal Deposit Insurance Corporation, Home Owners’ Loan Corporation, Farm Credit Administration, Federal Housing Administration, Federal Crop Insurance Corporation, Farmers’ Home Corporation, the Secretary of Agriculture acting through the Farmers’ Home Administration, or any land bank, intermediate credit bank, bank for cooperatives or any lending, mortgage, insurance, credit or savings and loan corporation or association authorized or acting under the laws of the United States or any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation, or any small business investment company, with intent to defraud any such institution or any other company, body politic or corporate, or any individual, or to deceive any officer, auditor, examiner or agent of any such institution or of department or agency of the United States, makes any false entry in any book, report or statement of or to any such institution, or without being duly authorized, draws any order or bill of exchange, makes any acceptance, or issues, puts forth or assigns any note, debenture, bond or other obligation, or draft, bill of exchange, mortgage, judgment, or decree, or with intent to defraud the United States or any agency thereof, or any corporation, institution, or association referred to in this section, participates or shares in or receives directly or indirectly any money, profit, property, or benefits through any transaction, loan, commission, contract, or any other act of any such corporation, institution, or association, shall be fined not more than \$10,000 or imprisoned not more than

five years, or both. (June 25, 1948, ch. 645, 62 Stat. 750; May 24, 1949, ch. 139, § 20, 63 Stat. 92; July 28, 1956, ch. 773, § 2, 70 Stat. 714; Aug. 21, 1958, Pub. L. 85-699, title VII, § 704, 72 Stat. 698; Oct. 4, 1961, Pub. L. 87-353, § 3(s), 75 Stat. 774.)

LEGISLATIVE HISTORY

Reviser's Note.—Based on sections 1026 (b) and 1514 (c) of title 7, U. S. C., 1940 ed., Agriculture, sections 264 (u), 984, 1121, 1138d (c), 1311, 1441 (c), 1467 (c) and 1731 (c) of title 12, U. S. C., 1940 ed., Banks and Banking, and section 616 (c) of title 15, U. S. C., 1940 ed., Commerce and Trade (Dec. 23, 1913, ch. 6, § 12B (u), as added June 16, 1933, ch. 89, § 8, 48 Stat. 178; July 17, 1916, ch. 245, § 31, fourth par., 39 Stat. 383; July 17, 1916, ch. 245, § 211 (a), as added Mar. 4, 1923, ch. 252, § 2, 42 Stat. 1459; Mar. 4, 1923, ch. 252, title II, § 216 (a), 42 Stat. 1471; Jan. 22, 1932, ch. 8, § 16 (c), 47 Stat. 11; July 22, 1932, ch. 522, § 21 (c), 47 Stat. 738; Ex. Ord. No. 6084, Mar. 27, 1933; June 13, 1933, ch. 64, § 8 (c), 48 Stat. 135; June 16, 1933, ch. 98, § 64 (c), 48 Stat. 268; Jan. 31, 1934, ch. 7, § 13, 48 Stat. 347; June 27, 1934, ch. 847, § 512 (c), 48 Stat. 1265; Aug. 23, 1935, ch. 614, § 101, 49 Stat. 701; July 22, 1937, ch. 517, title IV, § 52 (b), 50 Stat. 532; Feb. 16, 1938, ch. 30, title V, § 514 (c), 52 Stat. 76; Aug. 14, 1946, ch. 964, § 3, 60 Stat. 1064).

Each of the eleven sections from which this section was derived contained similar provisions relating to embezzlement, false entries, and fraudulent issuance or assignment of obligations with respect to one or more named agencies or corporations.

These were divided and the false entry and fraudulent issuance or assignment of obligation provisions of all form the basis of this section. The remaining provisions of each section, relating to embezzlement and misapplication, form the basis for section 657 of this title. That portion of said section 616 (c) of title 15, relating to disclosure of information, forms the basis for section 1904 of this title.

Each revised section condenses and simplifies the constituent provisions without change of substance except as herein indicated.

The punishment provisions in each section were the same except that in section 1026 (b) of title 7, U. S. C., 1940 ed., and sections 984, 1121, and 1311 of title 12, U. S. C., 1940 ed., the maximum fine was \$5,000. This consolidated section adopts the \$10,000 maximum fine provided by the seven other sections.

References to persons aiding or abetting contained in sections 984, 1121, and 1311 of title 12, U. S. C., 1940 ed., were omitted as unnecessary, as such persons are made principals by section 2 of this title.

The term "receiver," used in sections 1121 and 1311 of title 12, U. S. C., 1940 ed., with reference to Federal intermediate credit banks and agricultural credit corporations, was omitted as this term is undoubtedly embraced in the phrase "or connected in any capacity with."

The term "or of any department or agency of the United States" was inserted in order to clarify the sweeping provisions against fraudulent acts and to eliminate any possible ambiguity as to scope of section. (See definitions of "department" and "agency" in section 6 of this title.)

Words "shall be deemed guilty of a misdemeanor", contained in section 1311 of title 12, U. S. C., 1940 ed., were omitted as unnecessary, in view of definition of misdemeanor in section 1 of this title.

Words "and upon conviction", contained in section 1311 of title 12, U. S. C., 1940 ed., were omitted as surplusage, because punishment cannot be imposed until after conviction.

Words "in any district court of the United States", contained in section 1311 of title 12, U.S.C., 1940 ed., were omitted as unnecessary, because section 3231 of this title confers jurisdiction on the Federal district courts of all crimes and offenses defined in this title.

The conspiracy provisions of section 1138d(f) of title 12, U.S.C. 1940 ed., Banks and Banking, were not added to this consolidated section for reasons stated in reviser's note under section 493 of this title. (See also reviser's note under section 371 of this title.)

AMENDMENTS

1961—Pub. L. 87-353 struck out "Federal Farm Mortgage Corporation," following "Federal Housing Administration,".

1958—Pub. L. 85-699 included officers, agents or employees of or connected in any capacity with small business investment companies.

1956—Act July 28, 1956, included officers, agents or employees of or connected in any capacity with any institution the accounts of which are insured by the Federal Savings and Loan Insurance Corporation.

1949—Act May 24, 1949, inserted "the Secretary of Agriculture acting through the Farmers' Home Administration."

EXCEPTIONS FROM TRANSFER OF FUNCTIONS

Functions of the Corporations of the Department of Agriculture, the boards of directors and officers of such corporations; the Advisory Board of the Commodity Credit Corporation; and the Farm Credit Administration or any agency, officer or entity of, under, or subject to the supervision of the said Administration were excepted from the functions of officers, agencies and employees transferred to the Secretary of Agriculture by 1953 Reorg. Plan No. 2, § 1, eff. June 4, 1953, 18 F.R. 3219, 67 Stat. 633, set out as a note under section 511 of Title 5, Executive Departments and Government Officers and Employees.

ABOLITION OF HOME OWNERS' LOAN CORPORATION

For dissolution and abolishment of Home Owners' Loan Corporation, referred to this section, by act June 30, 1953, ch. 170, § 21, 67 Stat. 126, see note under section 1463 of Title 12, Banks and Banking.

FARM CREDIT ADMINISTRATION

Establishment of Farm Credit Administration as independent agency, and other changes in status, functions, etc., see section 636a et seq., of Title 12, Banks and Banking.

ABOLITION OF RECONSTRUCTION FINANCE CORPORATION

Section 6(a) of 1957 Reorg. Plan No. 1, eff. June 30, 1957, 22 F.R. 4633, 71 Stat. 647, set out as a note under section 601 of Title 15, Commerce and Trade, abolished the Reconstruction Finance Corporation.

CROSS REFERENCE

Financial control of government corporations, see Chapter 14 of Title 31, Money and Finance.

Secret Service, detection, arrest and delivery into custody of any person violating this section in so far as the Federal Deposit Insurance Corporation, Federal land banks, joint-stock land banks and national farm loan associations are concerned, see section 3056 of this title.

* * * * *

§ 1014. Loan and credit applications generally; renewals and discounts; crop insurance.

Whoever knowingly makes any false statement or report, or willfully overvalues any land, property or security, for the purpose of influencing in any way the action of the Reconstruction Finance Corporation, Farm Credit Administration, Federal Crop Insurance Corporation, Farmers' Home Corporation, the Secretary of Agriculture acting through the Farmers' Home Administration, any Federal intermediate credit bank, or any division, officer, or employee thereof, or of any corporation organized under sections 1131—1134m of Title 12, or of any regional agricultural credit corporation established pursuant to law, or of the National Agricultural Credit Corporation, a Federal Home Loan Bank, the Federal Home Loan Bank Board, the Home Owners' Loan Corporation, a Federal Savings and Loan Association, a Federal land bank, a joint-stock land bank, a Federal land bank association, a Federal Reserve bank, a small business investment company or a Federal credit union, upon any application, advance, discount, purchase, purchase agreement, repurchase agreement, commitment, or loan, or any change or extension of any of the same, by renewal, deferment of action or otherwise, or the acceptance, release, or substitution of security therefor, shall be fined not more than \$5,000 or imprisoned not more than two years, or both. (June 25, 1948, ch. 645, 62 Stat. 752; May 24, 1949, ch. 139, § 21, 63 Stat. 92; July 26, 1956, ch. 741, Title I, § 109, 70 Stat. 667; Aug. 21, 1958, Pub. L. 85-699, title VII, § 705, 72 Stat. 699; Aug. 18, 1959, Pub. L. 86-168, title I, § 104(h), 73 Stat. 387; Oct. 4, 1961,

Pub. L. 87-353, § 3(t), 75 Stat. 774; July 2, 1964, Pub. L. 88-353, § 5, 78 Stat. 269.)

LEGISLATIVE HISTORY

Reviser's Note.—Based on sections 1026(a) and 1514(a) of title 7, U.S.C., 1940 ed., Agriculture, sections 596, 981, 1122, 1123, 1138d (a), 1248, 1312, 1313, 1441 (a), and 1467 (a), of title 12, U.S.C., 1940 ed., Banks and Banking, and section 616 (a) of title 15, U.S.C., 1940 ed., Commerce and Trade (Dec. 23, 1913, ch. 6, § 22 (h), as added June 19, 1934, ch. 653, § 3, 48 Stat. 1107; July 17, 1916, ch. 245, § 31, first paragraph, 39 Stat. 382; July 17, 1916, ch. 245, § 211 (b) (c), as added Mar. 4, 1923, ch. 252, § 2, 42 Stat. 1460; Mar. 4, 1923, ch. 252, title II, §§ 209 (h), 216 (b) (c), 42 Stat. 1468, 1472; Jan. 22, 1932, ch. 8, § 16 (a), 47 Stat. 11; July 22, 1932, ch. 522, § 21 (a), 47 Stat. 738; June 13, 1933, ch. 64, § 8 (a), 48 Stat. 134; June 16, 1933, ch. 98, § 64 (a), 48 Stat. 267; Jan. 31, 1934, ch. 7, § 13, 48 Stat. 347; June 3, 1935, ch. 164, § 21, 49 Stat. 319; July 22, 1937, ch. 517, title IV, § 52 (a); 50 Stat. 531; Feb. 16, 1938, ch. 30, title V, § 514 (a), 52 Stat. 76; Aug. 14, 1946, ch. 964, § 3, 60 Stat. 1064).

Each of the 13 sections from which this section was derived contained similar provisions either relating to false representations and statements, or overvaluation of security, with respect to one or more of the named banks, agencies, or corporations.

These were consolidated and the false statement and security overvaluation provisions of all, form the basis of this section. The provisions of section 981 of title 12, U. S. C. 1940 ed., Banks and Banking, relating to acceptance of loans or gratuities by examiners, were consolidated with similar provisions from other sections to form section 218 of this title. The provisions of said section 981 of title 12, U.S.C., 1940 ed., Banks and Banking, prohibiting land bank and national farm loan association examiners from performing "any other service for compensation for any bank or banking or loan association, or for any person connected therewith in any capacity" were consolidated with similar provisions from other sections to form section 1909 of this title.

Eight of the consolidated sections contained identical punishment, each providing for a maximum fine of \$5,000 and maximum imprisonment of 2 years. Two sections provided for a maximum fine of \$10,000 and maximum imprisonment of 5 years. One section provided for maximum fine of \$5,000 and maximum imprisonment of 5 years, one section provided for maximum fine of \$2,000 and maximum imprisonment of 2 years, and one section provided for maximum fine of \$5,000 and maximum imprisonment of 1 year.

The punishment by maximum fine of \$5,000 or maximum imprisonment of 2 years, or both, provided in this consolidated section was adopted as most consistent with the greater number of comparable sections. (See sections 1008 and 1010 of this title.) This is a reasonable reconciliation of the conflicting punishment provisions and adequate for the offenses described.

The enumeration of "application, advance, discount, purchase, purchase agreement, repurchase agreement, commitment, or loan" and the wording "or any change or extension of any of the same, by renewal, deferment of action or otherwise, or the acceptance, release, or substitution of security therefor" does not occur in any one of the original sections, but such enumeration and such wording are adequate, and they represent a composite of terms and transactions mentioned in each.

In addition, changes were made in phraseology to secure uniformity of style, and some rephrasing was necessary, but the consolidation was without change of substance except as above indicated.

Section 1138d (f) of title 12, U.S.C., 1940 ed., Banks and Banking, relating to conspiracy, was not added to this consolidated section for reasons given in reviser's note under section 493 of this title.

REFERENCES IN TEXT

Sections 1131b and 1131g-1 of Title 12, included within the reference to sections 1131-1134m of Title 12, were repealed by act July 26, 1956, ch. 741, title 1, § 105(c), (q), 70 Stat. 665, 666.

Sections 1131, 1131a and 1131j of Title 12, included within the reference in text to sections 1131-1134m of Title 12 are omitted from the Code and are now covered, respectively, by sections, 1134, 1134a and 1131g-2 of Title 12, Banks and Banking.

AMENDMENTS

1964—Pub. L. 88-353 included Federal credit unions.

1961—Pub. L. 87-354 struck out "or the Federal Farm Mortgage Corporation," following "any Federal intermediate credit bank."

1959—Pub. L. 86-168 substituted "Federal land bank association" for "National farm loan association".

1958—Pub. L. 85-699 included small business investment companies.

1956—Act July 26, 1956, eliminated corporations in which a Production Credit Corporation holds stock.

1949—Act May 24, 1949, inserted "the Secretary of Agriculture acting through the Farmers' Home Administration".

EFFECTIVE DATE OF 1959 AMENDMENT

Amendment of section by Pub. L. 86-168 effective Dec. 31, 1959, see section 104(k) of Pub. L. 86-168, set out as a note under section 751 of Title 12, Banks and Banking.

EFFECTIVE DATE OF 1956 AMENDMENT

Amendment of this section by act July 26, 1956, effective Jan. 1, 1957, see section 202(a) of Act July 26, 1956, set out as a note under section 1027 of Title 12, Banks and Banking.

ABOLITION OF HOME OWNERS' LOAN CORPORATION

For dissolution and abolishment of Home Owners' Loan Corporation, referred to this section, by act June 30, 1953, ch. 170, § 21, 67 Stat. 126, see note under section 1463 of Title 12, Banks and Banking.

FARM CREDIT ADMINISTRATION

Establishment of Farm Credit Administration as independent agency, and other changes in status, functions, etc., see section 636a et seq., of Title 12, Banks and Banking.

ABOLITION OF RECONSTRUCTION FINANCE CORPORATION

Section 6(a) of 1957 Reorg. Plan No. 1, eff. June 30, 1957, 22 F.R. 4633, 71 Stat. 647, set out as a note under section 601 of Title 15, Commerce and Trade, abolished the Reconstruction Finance Corporation.

CROSS REFERENCES

Compromise, adjustment or cancellation of farm indebtedness, false statements, see section 1026 of this title.

Liability of directors and officers of member banks, see section 503 of Title 12, Banks and Banking.

Secret Service, detection, arrest and delivery into custody of any person violating this section in so far as the Federal land banks, joint-stock land banks and national farm loan associations are concerned, see section 3056 of this title.

(The following is a revised version of the bill prepared by the staff:)

[S. 3695, 89th Cong., 2d sess.]

AMENDMENT

(In the nature of a substitute)

To amend the Small Business Investment Act of 1958, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the Small Business Investment Act Amendments of 1966.

SEC. 2. Section 201 of the Small Business Investment Act of 1958 is amended to read as follows:

"ESTABLISHMENT OF SMALL BUSINESS INVESTMENT DIVISION

"SEC. 201. There is hereby established in the Small Business Administration a division to be known as the Small Business Investment Division. The Division shall be headed by an Associate Administrator who shall be appointed by the

Administrator, and shall receive compensation at the rate provided by law for other associate administrators of the Small Business Administration."

SEC. 3. Section 303 of the Small Business Investment Act of 1958 is amended by adding at the end thereof a new subsection as follows:

"(c) The Administration's share of any loan made under subsection (b) to any small business investment company, after the effective date of this subsection, shall become immediately due and payable whenever the Administration determines that such company has suffered an impairment of capital (as defined in regulations prescribed by the Administration), and gives written notice to such company of such determination."

SEC. 4. Section 308 of the Small Business Investment Act of 1958 is amended—

- (1) by striking out the last two sentences of subsection (c); and,
- (2) by inserting after subsection (e) the following new subsections:

"(f) In the performance of, and with respect to the functions, powers, and duties vested by this Act, the Administrator and the Administration shall (in addition to any authority otherwise vested by this Act) have the functions, powers, and duties set forth in the Small Business Act, and the provisions of sections 13 and 16 of that Act, insofar as applicable, are extended to the functions of the Administrator and the Administration under this Act.

"(g) The Administration shall include in its annual report to the Congress a full and detailed account of its operations under this Act. Such report shall set forth the amount of losses sustained by the Government as a result of such operations during the preceding fiscal year, together with an estimate of the total losses which the Government can reasonably expect to incur as a result of such operations."

SEC. 5. Section 310 of the Small Business Investment Act of 1958 is amended—

- (1) by striking out the section heading and inserting in lieu thereof "Examinations and Investigations"; and
- (2) by inserting "(a)" after "Sec. 310.", and by adding at the end thereof a new subsection as follows:

"(b) Each small business investment company shall be subject to examinations made by direction of the Administration by examiners selected or approved by the Administration, and the cost of such examinations, including the compensation of the examiners, may in the discretion of the Administration be assessed against the company examined and when so assessed shall be paid by such company. Every such company shall make such reports to the Administration at such times and in such form as the Administration may require; except that the Administration is authorized to exempt from making such reports any such company which is registered under the Investment Company Act of 1940 to the extent necessary to avoid duplication in reporting requirements."

SEC. 6. (a) Section 309 of the Small Business Investment Act of 1958 is amended by striking out the section heading and inserting in lieu thereof the following:

"REVOCATION AND SUSPENSION OF LICENSES; CEASE AND DESIST ORDERS

"(b) Section 309 (a) of such Act is amended—

- "(1) by inserting 'revoked or' before 'suspended';
- "(2) by striking out in paragraph (1) 'Administration, for the purpose of obtaining the license' and inserting in lieu thereof 'Administration'; and
- "(3) by striking out in paragraph (2) 'for the purpose of obtaining the license.'"

(c) Section 309 (b) of such Act is amended to read as follows:

"(b) Where a licensee or any other person has not complied with any provision of this Act, or of any regulation issued under this Act by the Administration, or is engaging or is about to engage in any acts or practices which constitute or will constitute a violation of such Act or regulation, the Administration may order such licensee or other person to cease and desist from such action or failure to act. The Administration may further order such licensee or other person to take such action or to refrain from such action as the Administration deems necessary to insure compliance with the Act and the regulations. The Administration may also suspend the license of a licensee, against whom an order has been issued, until such licensee complies with such order."

d) Section 309(c) of such Act is amended—

(1) by inserting after "licensee", each place it appears, the following: "or other person"; and

(2) by inserting before "suspending", each place it appears, the following: "revoking or".

(e) Section 309(e) of such Act is amended by inserting after "licensee", the first place it appears, the following: "or other person against whom an order is issued".

(f) Section 309(f) of such Act is amended—

(1) by striking out the first sentence and inserting in lieu thereof the following: "If any licensee or other person against which or against whom an order is issued under this section fails to obey the order, the Administration may apply to the United States court of appeals, within the circuit where the licensee has its principal place of business, for the enforcement of the order, and shall file a transcript of the record upon which the order complained of was entered."; and

(2) by inserting "or other person" before the period at the end of the second sentence.

SEC. 7. Section 311 of the Small Business Investment Act of 1958 is amended by adding at the end thereof the following new subsection:

"(c) The Administration shall have authority to act as trustee or receiver of the licensee. Upon request by the Administration, the court may appoint the Administration to act in such capacity unless the court deems such appointment inequitable or otherwise inappropriate by reason of the special circumstances involved."

SEC. 8. The Small Business Investment Act of 1958 is further amended by adding at the end thereof the following new sections:

"REMOVAL OR SUSPENSION OF DIRECTORS AND OFFICERS OF LICENSEES

"SEC. 313. (a) Whenever, in the opinion of the Administration, any director or officer of a licensee has committed any violation of this Act, or any regulation issued thereunder, or of a cease-and-desist order which has become final, or has committed or engaged in any act, omission, or practice which constitutes a breach of his fiduciary duty as such director or officer, and the Administration determines that the licensee has suffered or will probably suffer substantial financial loss or other damage or that the interests of the Administration could be seriously prejudiced by reason of such violation or practice or breach of fiduciary duty, and that such violation or practice or breach of fiduciary duty is one involving personal dishonesty on the part of such director or officer, the Administration may serve upon such director or officer a written notice of its intention to remove him from office.

"(b) In respect to any director or officer referred to in subsection (a), the Administration may, if it deems it necessary for the protection of the licensee or the interests of the Administration, by written notice to such effect served upon such director or officer, suspend him from office and/or prohibit him from further participation in any manner in the conduct of the affairs of the licensee. Such suspension and/or prohibition shall become effective upon service of such notice and, unless stayed by a court in proceedings authorized by subsection (d) of this section, shall remain in effect pending the completion of the administrative proceedings pursuant to the notice served under subsection (a) and until such time as the Administration shall dismiss the charges specified in such notice, or, if an order of removal and/or prohibition is issued against the director or officer or other person, until the effective date of any such order. Copies of any such notice shall also be served upon the interested licensee.

"(c) A notice of intention to suspend or remove a director or officer, and/or to prohibit his participation in the conduct of the affairs of a licensee, shall contain a statement of the facts constituting grounds therefor, and shall fix a time and place at which a hearing will be held thereon. Such hearing shall be fixed for a date not earlier than thirty days nor later than sixty days after the date of service of such notice, unless an earlier or a later date is set by the Administration at the request of (i) such director or officer and for good cause shown, or (ii) the Attorney General of the United States. Unless such director or officer shall appear at the hearing in person or by a duly authorized representative, he

shall be deemed to have consented to the issuance of an order of such removal and/or prohibition. In the event of such consent, or if upon the record made at any such hearing the Administration shall find that any of the grounds specified in such notice has been established, the Administration may issue such orders of suspension or removal from office, and/or prohibition from participation in the conduct of the affairs of the licensee, as it may deem appropriate. Any such order shall become effective at the expiration of thirty days after service upon licensee and the director or officer concerned (except in the case of an order issued upon consent, which shall become effective at the time specified therein). Such order shall remain effective and enforceable except to such extent as it is stayed, modified, terminated, or set aside by action of the Administration or a reviewing court.

“(d) Within ten days after any director or officer has been suspended from office and/or prohibited from participation in the conduct of the affairs of a licensee under subsection (b), such director or officer may apply to the United States district court for the judicial district in which the home office of the licensee is located, or the United States District Court for the District of Columbia, for a stay of such suspension and/or prohibition pending the completion of the administrative proceedings pursuant to the notice served upon such director or officer under subsection (a), and such court shall have jurisdiction to stay such suspension and/or prohibition.

“(e) Whenever any director or officer of a licensee is charged in any information, indictment, or complaint authorized by a United States Attorney, with the commission of or participation in a felony involving dishonesty or breach of trust, the Administration may, by written notice served upon such director or officer, suspend him from office and/or prohibit him from further participation in any manner in the conduct of the affairs of the licensee. A copy of such notice shall also be served upon the licensee. Such suspension and/or prohibition shall remain in effect until such information, indictment, or complaint is finally disposed of or until terminated by the Administration. In the event that a judgment of conviction with respect to such offense is entered against such director or officer, and at such time as such judgment is not subject to further appellate review, the Administration may issue and serve upon such director or officer, an order removing him from office and/or prohibiting him from further participation in any manner in the conduct of the affairs of the licensee except with the consent of the Administration. A copy of such order shall be served upon such licensee, whereupon such director or officer shall cease to be a director or officer of such licensee. A finding of not guilty or other disposition of the charge shall not preclude the Administration from thereafter instituting proceedings to remove such director, officer, or other person from office and/or to prohibit further participation in licensee affairs, pursuant to subsections (a) or (b).

“(f) (1) Any hearing provided for in this section shall be held in the Federal judicial district or in the territory in which the principal office of the licensee is located unless the party afforded the hearing consents to another place, and shall be conducted in accordance with the provisions of the Administrative Procedure Act; but such hearing shall be private, unless a public hearing is agreed to by the party afforded the hearing and by the Administration. After such hearing, and within ninety days after the Administration has notified the parties that the case has been submitted to it for final decision, the Administration shall render its decision (which shall include findings of fact upon which its decision is predicated) and shall issue and cause to be served upon each party to the proceeding an order or orders consistent with the provisions of this section. Judicial review of any such order shall be exclusively as provided in this subsection. Unless a petition for review is timely filed in a court of appeals of the United States, as hereinafter provided in paragraph (2) of this subsection, and thereafter until the record in the proceeding has been filed as so provided, the Administration may at any time, upon such notice and in such manner as it shall deem proper, modify, terminate, or set aside any such order. Upon such filing of the record, the Administration may modify, terminate, or set aside any such order with permission of the court.

“(2) Any party to such proceeding may obtain a review of any order served pursuant to paragraph (1) of this subsection (other than an order issued with the consent of the director or officer concerned, or an order issued under sub-

section (e) of this section), by filing in the court of appeals of the United States for the circuit in which the principal office of the licensee is located, or in the United States Court of Appeals for the District of Columbia Circuit, within thirty days after the date of service of such order, a written petition praying that the order of the Administration be modified, terminated, or set aside. A copy of such petition shall be forthwith transmitted by the clerk of the court to the Administration, and thereupon the Administration shall file in the court the record in the proceeding, as provided in section 2112 of title 28 of the United States Code. Upon the filing of such petition, such court shall have jurisdiction, which upon the filing of the record shall, except as provided in the last sentence of said paragraph (1), be exclusive, to affirm, modify, terminate, or set aside, in whole or in part the order of the Administration. Review of such proceedings shall be had as provided in the Administrative Procedure Act. The judgment and decree of the court shall be final except that the same shall be subject to review by the Supreme Court upon certiorari as provided in section 1254 of title 28 of the United States Code.

"(3) The commencement of proceedings for judicial review under paragraph (2) of this subsection shall not, unless specifically ordered by the court, operate as a stay of any order issued by the Administration.

"UNLAWFUL ACTS AND OMISSIONS BY OFFICERS, DIRECTORS, EMPLOYEES, OR AGENTS;
BREACH OF FIDUCIARY DUTY

"SEC. 314. (a) Wherever a licensee violates any provision of this Act or regulation issued thereunder by reason of its failure to comply with the terms thereof or by reason of its engaging in any act or practice which constitutes or will constitute a violation thereof, such violation shall be deemed to be also a violation and an unlawful act on the part of any person, including the individual officers, directors, or employees or agents of such licensee who, directly or indirectly, authorizes, orders, participates in, or causes, brings about, counsels, aids or abets in the commission of any acts, practices or transactions which constitute or will constitute, in whole or in part, such violation.

"(b) It shall be unlawful for an officer, director, employee, agent or other participant in the management or conduct of the affairs of the licensee to engage in any act or practice, or to omit any act, in breach of his fiduciary duty as such officer, director, employee, agent or participant in the management or conduct of the affairs of the licensee if, as a result thereof, the licensee has suffered or is in imminent danger of suffering financial loss or other damage.

"(c) Except with the written consent of the Administration, it shall be unlawful (1) for any person to hereafter take office as an officer, director, employee, or agent or participant in the conduct of the affairs or management of a licensee who has been convicted of any felony or any criminal offense involving dishonesty or a breach of trust, or who has been found civilly liable in damages, or has been permanently or temporarily enjoined by an order, judgment or decree of any court of competent jurisdiction, by reason of any act or practice involving fraud or breach of trust; or (2) for any person to continue to serve in any of the above capacities described in this subsection who is hereafter convicted of any felony or criminal offense involving dishonesty or breach of trust, or who is hereafter found civilly liable in damages, or permanently or temporarily enjoined by an order, judgment or decree of any court of competent jurisdiction, by reason of any act or practice involving fraud or breach of trust.

"PENALTIES AND FORFEITURES

"SEC. 215. A licensee which violates any regulation or written directive issued by the Administrator, requiring the filing of any regular or special report pursuant to section 310 (b) of this Act, shall forfeit and pay to the United States a civil penalty of not more than \$100 for each and every day of the continuance of the licensee's failure to file such report, unless it is shown that such failure is due to reasonable cause and not due to willful neglect. The civil penalties provided for in this section shall accrue to the United States and may be recovered in a civil action brought by the United States: *Provided*, That the Administration may by rules and regulations, or upon application of an interested party, at any time previous to such failure, by order, after notice and opportunity for hearing, exempt in whole or in part, any small business investment company from the

provisions of this section, upon such terms and conditions and for such period of time as it deems necessary and appropriate, if the Administration finds that such action is not inconsistent with the public interest or the protection of the Administration. The Administration may for the purposes of this section make any alternative requirements appropriate to the situation.

"JURISDICTION AND SERVICE OF PROCESS

"SEC. 316. Any suit or action brought under section 308, 311, or 315 by the Administration at law or in equity to enforce any liability or duty created by, or to enjoin any violation of this Act or rules or regulations or orders promulgated thereunder, shall be brought in the district wherein the licensee maintains its principal office, and process in such cases may be served in any district in which the defendant maintains its principal office or, transacts business, or wherever the defendant may be found."

SEC. 9. (a) Section 4 (b) of the Small Business Act is amended by striking out "three Deputy Administrators" and inserting in lieu thereof "a Deputy Administrator and three Associate Administrators."

(b) Such section is further amended by adding at the end thereof the following: "The Deputy Administrator shall be Acting Administrator of the Administration during the absence or disability of the Administrator or in the event of a vacancy in the office of the Administrator."

(c) (1) Section 303 (d) of the Federal Executive Salary Act of 1964 is amended by adding at the end thereof the following:

"(70) Deputy Administrator of the Small Business Administration."

(2) Section 303 (e) (11) of such Act is amended by striking out "Deputy Administrators of the Small Business Administration (4)" and inserting in lieu thereof "Associate Administrators of the Small Business Administration (3)."

SEC. 10. (a) Chapter 17 of title 18, United States Code, is amended by adding at the end thereof a new section as follows:

"§ 338. Stock of small business investment companies as collateral for loans.

"Whoever, being an officer, director, or principal shareholder of any small business investment company which is licensed under the provisions of the Small Business Investment Act of 1958, knowingly offers any shares of stock in such company as security for any loan to purchase an interest in such company, shall be fined not more than \$10,000 or imprisoned not more than one year, or both.

"As used in this section, the term 'principal shareholder' of any small business investment company means a person who directly or indirectly owns, controls, or holds with power to vote, 10 per centum or more of the outstanding voting shares of such company.

"This section shall not be construed to apply to any loan made prior to the effective date of this section, unless, after the expiration of thirty days after such date, such loan is secured in whole or in part by collateral consisting of shares of stock in any such company."

(b) The analysis to chapter 17 of title 18, United States Code, is amended by adding at the end thereof a new item as follows:

"§ 338. Stock of small business investment companies as collateral for loans.

SEC. 11. (a) The table of contents of the Small Business Investment Act of 1958 is amended—

(1) by striking out the items describing the contents of sections 309 and 310 and inserting in lieu thereof the following:

"SEC. 309. Revocation and suspension of licenses; cease and desist orders.

"SEC. 310. Examinations and investigations." and

(2) by inserting at the end of that part which describes the contents of title III the following new items:

"SEC. 313. Removal or suspension of directors and officers of licensees.

"SEC. 314. Unlawful acts and omissions by officers, directors, employees, or agents; breach of fiduciary duty.

"SEC. 315. Penalties and forfeitures.

"SEC. 316. Jurisdiction and service of process."

