Alan Belkin
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DECISION

THE COMPTROLLER GENERAL
OF THE UNITED STATES
WASHINGTON, D.C. 20548

FILE: B-149685 DATE: February 3, 1977

MATTER OF: Eligibility of SBICs to participate as lenders in guaranteed loan programs of SBA and FmHA.

DIGEST: Small business investment companies (SBICs) are not eligible to participate as guaranteed lenders in either Small Business Administration's (SBA) or Farmers Home Administration's (FmHA) loan programs. As stated in 49 Comp. Gen. 32, legislative history of Small Business Investment Act demonstrates congressional intent that SBICs operate independently of other Government loan programs. Nothing in SBIC Act or Consolidated Farm and Rural Development Act, which established FmHA's authority to guarantee loans, or legislative history of either, supports SBA's position that SBIC's should now be permitted to participate as guaranteed lenders in these loan programs.

This decision to the Administrator of the Small Business Administration (SBA) is in response to his request for our legal opinion as to the eligibility of small business investment companies (SBICs) to participate as guaranteed lenders in both SBA's section 7(a) Guaranteed Loan program and the Farmers Home Administration (FmHA) Business and Industrial Loan program. Each of these questions will be considered separately.

Section 7(a) of the Small Business Act, as amended, 15 U.S.C. § 636(a)(1970), provides that SBA may make loans to small business concerns "* * * either directly or in cooperation with banks or other lending institutions through agreements to participate on an immediate or deferred basis." Basically, the question before us is whether or not SBICs established under the authority of the Small Business Investment Act of 1958, as amended, 15 U.S.C. §§ 661 et seq., can qualify as "other lending institutions" under section 7(a) of the Small Business Act, supra. SBICs were established for the purposes of providing a source of equity capital to small business concerns, as well as the making of loans to such concerns, in order to provide them with the funds needed for sound financing, growth, modernization, and expansion. See 15 U.S.C. §§ 684(a) and 685(a) (1970 and Supp. V, 1975). Also, section 305(b) of the Small Business Investment Act, as amended, 15 U.S.C. § 685(b)(1970), provides that loans may be made by SBICs "directly or in cooperation with other lenders, incorporated or unincorporated, through agreements to participate on an immediate or deferred basis."

As pointed out in SBA's submission, our Office considered the question of whether SBICs could participate as guaranteed lenders under section 7(a) of the Small Business Act in our decision 49 Comp. Gen. 32 (1969) and we concluded that the Small Business Investment Act must be construed as precluding SBICs from participating with SBA in making loans to small business concerns. However, it is SBA's view that the present intent of SBA and the specific factual situation with respect to such proposed loans are so different from its 1969 proposal as to justify reconsideration of that decision. In this regard SBA's submission reads in pertinent part as follows:

> "First, our intent is not to interlock or piggyback Government programs for the small business sector but rather the intent is to put a velocity factor or multiplier behind presently existing funds in order to channel and expand the total flow of available financing.
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> "The basic intent is that SBIC's be permitted to originate SBA 7(a) loans just as banks now do but in contrast to banks, the SBA 7(a) guarantee would only run to the SBIC's for the time that it takes to sell the guaranteed portions to passive institutional and other investors while the SBIC would remain as servicing agent for the secondary participant. This is how the impact of presently available funds could be increased by a velocity factor.
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> "SBIC's would benefit from such a program since additional servicing income would be available, therefore, SBA anticipates requiring a quid pro quo from participating SBIC's. For example, SBA might require SBIC's to originate SBA-guaranteed loans to firms in the manufacturing sector (job creation potential), or SBA might require SBIC's to maintain a certain level or proportion of their other investments in equity interests of small business concerns which it does not now do.
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> "SBA would, of course, promulgate regulations which would tightly control SBIC activities so that no abuses such as conflicts of interest could arise."

Our 1969 decision that SBICs could not participate with SBA in making guaranteed loans to small business concerns was based on several factors. We relied primarily on the legislative history of the Small Business Investment Act, which was quoted extensively in our decision. We noted, for example, that the SBIC program was to "be launched with a minimum of Federal activity and with only a modest increase in personnel and administrative expenditures by the Small Business Administration," and was "to operate and be accounted for in complete separation from other Federal small business programs." See S. Rep. No. 1652, 85th Cong., 2d Sess. 2, 3 (1958).

Another factor that we relied upon in reaching our conclusion was the unsuccessful legislative attempt in 1961 to amend section 305(b) of the Small Business Investment Act, supra, to specifically include SBA among the "other lenders" referred to therein. In our decision we quoted from the testimony of the then Administrator of SBA who had opposed the proposed amendment on the following grounds:

> "Section 6 of the bill would amend section 305(b) of the act so as to authorize SBIC's to make loans to small business concerns directly or in cooperation with 'other lenders, public or private, incorporated or unincorporated, including the Small Business Administration' through agreements to participate on an immediate or deferred basis.
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> "Under the existing provisions of section 305(b) of the act, SBIC's can make loans on a cooperative basis--but only with lending 'institutions.' I have no objections to section 6 of the bill insofar as it would extend coverage to individual lenders and other lenders which do not qualify as lending institutions.
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> "However, I do not favor the proposal of section 6 that SBIC's be authorized to extend loans to small business concerns in cooperation with the Small Business Administration.
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> "I would like to emphasize the difference in the lending functions of SBIC's and those of SBA. The maximum maturity of SBA business loans is fixed by statute at 10 years. The small business investment program was not established for the purpose of providing such financing for small business. At the

time the Small Business Investment Act of 1958 was enacted, it was observed that, on the whole, the short-term and intermediate-term credit needs of small business were being met through existing facilities, private and governmental.

"The primary purpose of the lending authority delegated under the act to SBIC's is to provide small business concerns with long-term credit which cannot be obtained from SBA--with loans of maturities in excess of 10 years. If SBIC's are to fulfill the mission intended for them by Congress, they must concentrate their efforts in this area.

"By regulation, SBA could have confined SBIC loans to maturities of more than 10 years. However, this appeared to be too rigid a restriction, and to provide SBIC's with reasonable leeway a minimum maturity of 5 years was established on their loans.

"SBIC's should, as far as possible, avoid this zone of overlap. In any case, they should not be attracted into it with offers of SBA participation." (Emphasis added.)

Thus, it was apparent as pointed out in our decision, that the then Administrator of SBA believed that without the proposed amendment SBICs would not be authorized to extend loans to small business concerns in cooperation or in participation with SBA.

In reaching our conclusion we considered it to be very persuasive, and continue to do so, that Congress, although aware of SBA's long-standing position that the Small Business Investment Act did not allow SBIC's to participate with SBA in making loans to small business concerns and although provided with the opportunity to amend the Act so as to expressly allow such joint participation, chose to delete the proposed amendment from the bill. In our view this action clearly demonstrated the legislative intent that SBA and SBIC's should not participate together in making loans to small businesses.

The intent of the instant proposal by SBA may be somewhat different from the original proposal in that the SBIC would originate the loan but would then presumably sell the guaranteed portion thereof to another lending institution while remaining the servicing agent for the secondary participant. However, in light of the various statements in the legislative history of the Small Business Investment Act indicating that it was intended that SBICs operate completely independently of other Federal small business programs, which formed the primary basis for our earlier decision, we do not believe that any such differences between the two proposals are sufficient to justify a change in our position. It remains clear that under the present proposal the SBIC program would be operating in conjunction with the 7(a) program, both in the initial stage when the loan was made by the SBIC and thereafter while the SBIC continued to act as the servicing agent for the SBA guaranteed loan. Accordingly, it is and remains our view that, in the absence of legislation similar to that proposed in 1961 expressly authorizing SBA to participate with SBICs in making loans to small business concerns, it is impermissible for SBICs to participate with SBA as guaranteed lenders under the 7(a) program.

The other question presented in SBA's submission concerns the eligibility of SBICs to participate as guaranteed lenders in FmHA's Business and Industrial Loan program. The authority of FmHA to guarantee such loans is set forth in section 310B of the Consolidated Farm and Rural Development Act, as amended, 7 U.S.C. § 1932 (Supp. V, 1975), which provides in pertinent part as follows:

> "(a) The Secretary [of Agriculture] may also make and insure loans to public, private, or cooperative organizations organized for profit or nonprofit, to Indian tribes on Federal and State reservations or other federally recognized Indian tribal groups, or to individuals for the purpose of improving, developing, or financing business, industry, and employment and improving the economic and environmental climate in rural communities, including pollution abatement and control. Such loans, when originated, held, and serviced by other lenders, may be guaranteed by the Secretary under this section * * *."

On December 11, 1975, FmHA promulgated revised regulations outlining the substantive procedures for FmHA guaranteed Business and Industrial loans in rural areas. See 40 Fed. Reg. 57643 (1975), now codified at 7 CFR §§ 1980.401 et seq. (1976).

According to the revised regulatory provisions, SBICs are specifically included in the list of eligible lenders. See 7 CFR § 1980.419(b)(1). The United States, acting through FmHA, will guarantee up to 90 percent of such Business and Industrial loans that are made and serviced by eligible lenders.

On February 11, 1976, SBA advised all licensed SBICs that after reviewing the matter:

> ". . .[I]t is SBA's position that the B&I loan program does not fall within the functions and activities contemplated by the Small Business Investment Act [see Section 301(a) thereof, 15 U.S.C. 681(a)]. Accordingly, Licensees are hereby notified that participation in this program will be deemed a violation of such Act, and of the relevant regulation [13 C.F.R. § 107.303] thereunder."

The basis for SBA's position in this regard was articulated in an opinion of SBA's Acting General Counsel which concluded that there was no legal authority in the Consolidated Farm and Rural Development Act, or in the Small Business Investment Act, or in the legislative history of either, to support the participation by SBICs as guaranteed lenders in FmHA's loan program. To some extent this opinion also relied on both the rejection by Congress of the proposed amendment to the Small Business Investment Act in 1961 which would have expressly authorized SBICs to participate with other lenders both public and private, as well as our decision 49 Comp. Gen. 32 supra.

SBA has now expressed some doubt as to the correctness of its initial position that SBICs are precluded from making loans that would be guaranteed by FmHA. In this regard SBA's submission reads in pertinent part as follows:

> "First, while the SBA Administrator's testimony (quoted in the attached opinion) opposed the participation of any Federal agency with SBIC's in financing small concerns, your opinion focused entirely on SBA participation and concluded that you could not
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> > 'concur with [our] proposal to authorize SBICs to participate with SBA in loans to small business concerns'- [49 Comp. Gen. at 37].

"Therefore, to the extent that our position relied on your decision, such reliance may have been misplaced.

"Second, did Congress, in the 1972 legislation establishing FmHA's B&I program, intend to vest in FmHA authority to guarantee SBIC loans? If so, such authority is not based on any explicit provision of the Consolidated Farm and Rural Development Act, but must rest on an interpretive implication drawn from the general language of the 1972 law.

"Third, should our position be different if the SBIC would retain only the unguaranteed portion of the B&I loan, and sell at the closing of the loan, or immediately thereafter, the guaranteed portion to non-SBIC investors? We are advised that, as a practical matter, SBIC's are not interested in retention of the guaranteed portion, but are interested in the profit and income that they may derive from the sale of the guaranteed portion, and from the servicing of the loan, and from incidental services such as management advice [Sec. 308(b) of the Small Business Investment Act, 15 U.S.C. 687(b)].

"Fourth, prior to the publication by FmHA of its revised B&I regulations, when our attention had not focused on the broader implications of FmHA guaranties, SBA advised one Licensee, Cameron-Brown Capital Corporation, on March 18, 1975, that 'Such [guaranteed] investment is not prohibited under the SBI Act or Regulations.' * * * Moreover, SBA's then Acting Administrator, Mr. Laun, Deputy Administrator, advised the Office of Management and Budget on December 22, 1975, of the recently published FmHA regulation and wrote:

> 'There is nothing in the Small Business Investment Act of 1958, as amended, nor in the regulations promulgated thereunder to prohibit such guaranty, by F[m]HA. . . . This business and industrial loan program adopted by F.H.A. is beneficial to small business in rural areas and, of course, is most advantageous to SBICs.'

"It can thus be seen that SBA's position in the past has not been entirely consistent."

Having considered this question, we conclude that the initial position adopted by SBA--that there is no legal authority to support the participation of SBICs in FmHA's guaranteed loan program--is correct. First, as noted previously, the Small Business Investment Act, which authorized the establishment of SBICs, did not contemplate that they would participate in small business programs of other Government agencies. This exclusion from participation in other Federal small business programs would apply equally to FmHA's programs as to SBA's section 7(a) program under the reasoning of our 1969 decision.

Moreover, with respect to the question of whether Congress enacted the Consolidated Farm and Rural Development Act with the intent that FmHA be permitted to guarantee SBIC loans, we have found no support for such an interpretation, either in the actual language of the Act of its legislative history. As to the possibility of "an interpretive implication drawn from the general language of" that Act, we do not believe that such an implication exists. Even if it did, such an implication based on the general statutory language would be insufficient to counter the clear expression of legislative intent from the Small Business Investment Act that SBICs operate independently of other Government agencies.

For the reasons discussed previously with respect to proposed SBIC participation in SBA loans, it makes no difference that the SBICs would retain only the unguaranteed portion of the FmHA Business and Industrial loan and sell at the closing of the loan, or immediately thereafter, the guaranteed portion, to non-SBIC investors. Even under this type of arrangement the SBIC would be a participant in the loan program of another Government agency, thereby engaged in activities not contemplated by the Small Business Investment Act, and would be making and servicing loans which were intended to achieve purposes other than, or at least in addition to, those contemplated by that Act, thereby violating the statutory language and intent.

Finally, we do not believe it to be particularly significant that SBA's position in regard to the legality of this practice has not been entirely consistent and since the position we have adopted here was independently arrived at and is based on our own analysis.

In accordance with the foregoing, it is our opinion that SBICs are not eligible to participate as guaranteed lenders in either SBA's 7(a) loan program or FmHA's Business and Industrial loan program. Accordingly, FmHA should revise its regulations (7 CFR § 1980.419(b)) to remove SBICs from the list of lenders that are eligible to participate in its guaranteed loan program.

Deputy Comptroller General
of the United States