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SMALL BUSINESS INVESTMENT EXPANSION ACT OF 2007

SEPTEMBER 25, 2007.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Ms. VELÁZQUEZ, from the Committee on Small Business, submitted the following

R E P O R T

[To accompany H.R. 3567]

[Including cost estimate of the Congressional Budget Office]

The Committee on Small Business, to whom was referred the bill (H.R. 3567) to amend the Small Business Investment Act of 1958 to expand opportunities for investments in small businesses, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

CONTENTS

		Page
I.	Purpose and Summary	1
II.	Background and Need for Legislation	3
III.	Hearings	10
IV.	Committee Consideration	10
V.	Committee Votes	11
VI.	Section-by-Section Analysis of H.R. 3567	11
VII.	Congressional Budget Office Cost Estimate	20
VIII.	Committee Estimate of Costs	23
IX.	Oversight Findings	23
X.	Statement of Constitutional Authority	24
XI.	Compliance With Public Law 104–4	24
XII.	Congressional Accountability Act	24
XIII.	Federal Advisory Committee Statement	24
XIV.	Statement of No Earmarks	24
XV.	Performance Goals and Objectives	24
XVI.	Changes in Existing Law Made by the Bill, as Reported	24

I. PURPOSE AND SUMMARY

The Small Business Investment Expansion Act of 2007 is aimed at three broad goals. First, the bill will update and streamline

59–006

three programs in the Small Business Investment Act of 1958, the Small Business Investment Company (SBIC), New Markets Venture Capital (NMVC) and Surety Bond programs. Second, the bill will leverage a new investment strategy, angel investing, to direct more venture capital toward early stage and startup businesses. Finally, the bill will revise SBA rules that inhibit the free flow of venture capital investment to small businesses.

To streamline the SBIC program, this legislation will simplify the current method of calculating maximum leverage caps in favor of a straightforward maximum leverage cap that will remain workable for years to come. The bill will also revise limitations on aggregate investments to establish limitations that are more consistent with industry accepted portfolio risk management practices. Additional provisions of the bill will increase overall investment in smaller enterprises and will also establish incentives to form SBIC funds focused on investment in minority and women owned businesses. The New Markets Venture Capital program will also be updated with provisions that emphasize expanding the program and provide additional incentives for investment in small manufacturing companies in low-income areas. The final approval process for conditionally approved NMVC companies will be streamlined by establishing simplified application documents and permitting conditionally approved NMVC companies to receive funding for operational assistance. The operational assistance aspect will also be improved by eliminating the requirement that NMVC companies raise matching commitments prior to final approval and by simplifying the process for operational grant assistance. Finally, appropriations for the NMVC program will be authorized in a total amount of $35 million ($30 million to support debentures and $5 million for operational assistance grants), of which not less than one quarter must be used to support NMVC companies that invest primarily in small manufacturers.

The bill will also establish a new Office of Angel Investment within the SBA's Investment Division. This office will be headed by a Director of Angel Investment and will focus on three initiatives to increase equity investment in small businesses.

First, an Angel Investment Program will be established to provide eligible angel groups that have ten or more angel investors with matching financing leverage. This leverage will be used to finance early stage small businesses, with priority in financing going to angel groups that invest in small businesses controlled by veterans, women, or socially and economically disadvantaged small businesses. This leverage will be repaid to the SBA with a pro rata share of returns from the investment. Appropriations for the purpose of providing leverage to angel groups will be authorized in a total amount of $50 million.

Second, a directive will be established within the Office of Angel Investment to create a Federal Angel Network. This network will be a searchable directory of angel groups available on through the SBA's internet website. Additionally, the directory could be distributed or used by other networks to increase its exposure. The directory will include the names and contact information for angel groups and angel investors and will provide information about the types of investments each group or investor has made. One million

dollars will be authorized to be appropriated for the establishment of the angel network.

The Angel Investment Program will also include, a grant initiative to provide eligible state, federal, and nonprofit entities with resources to increase awareness and education about angel investing. As a condition of receiving grant assistance, however, eligible entities must provide 50 percent matching contributions, thus amplifying the benefits of grant assistance. This provision will bring more attention to the benefits of angel investing and attract more angel investors to participate in the program. A total of $4.5 million will be authorized for appropriations to carry out this initiative.

The bill will also address deficiencies in the Surety Bond program. The maximum permissible bond amount will be increased by half to $3 million. The bill will also strengthen surety companies' confidence in the Plan A program by barring the SBA from denying indemnity on Plan A guaranties based upon information that was provided as part of the guaranty application. The SBA will also be required to conduct a study on the program's current funding structure and report its findings to Congress within 180 days of the bill's enactment. The bill will make the Surety Bond program more affordable to small businesses and surety companies by providing the SBA with authority to contribute funds for the purpose of reducing the burden associated with surety and contractor fees on bond guarantees.

Finally, the bill modifies the Small Business Act to exclude venture capital investment in SBA's consideration of whether a firm is small for the purposes of the Act. The provision provides that when calculating the number of employees of a small business concern that has venture capital investment, the SBA will exclude those employees who work for companies affiliated with the venture capital company. The bill requires that the venture capital company comply, as appropriate, with federal registration requirements for investment companies. In addition, the bill prevents a venture capital that is controlled by a large business or a venture capital company with more than 500 employees from being recognized as a venture capital company under this provision.

II. Background and Need for Legislation

The Small Business Investment Company (SBIC) program is the SBA's primary capital investment program. It is the agency's largest and most important in terms of number of investments made and program level supported. The SBA does not make direct investments in small business concerns through the SBIC program, but instead licenses Small Business Investment Companies (SBICs) to administer the program.

SBICs are state-chartered entities organized solely for the purpose of providing a source of equity capital for small business concerns. The SBA provides funding to qualified SBICs with expertise in certain sectors or industries, which then use their own funds, plus resources borrowed with an SBA guaranty or "leverage," to invest in small businesses. Although subject to SBA regulation, SBICs remain privately owned and managed and make their own decisions about which small businesses investments to make.

The SBA provides leverage to SBICs in two forms, "debentures" and "participating securities." To obtain leverage, SBICs issue debentures or participating securities, which are guaranteed by the SBA. Separate pools of either SBA-guaranteed debentures or participating securities are formed and sold to investors through periodic securities offerings. An SBIC's business plan and investment strategy are the primary factors in determining the type of leverage used by the SBIC.

Both debentures and participating securities operate on a zero-subsidy basis, being funded by fixed commitment and drawdown fees as well as by annual fees based on a subsidy rate determined at the time of the commitment. The primary difference between debentures and participating securities, however, is the timing in repayment of leverage. Unlike debentures, which have a fixed time for repayment, participating securities leverage is repaid only out of profits of the SBIC fund, enabling the SBA to share in the profits of a participating securities SBIC.

Debenture SBICs have defined interest obligations to the SBA. Thus, they tend to focus on investing in companies that are mature enough to make current interest payments on the investment. Because interest can accrue on participating securities obligations, however, the participating securities program is better suited for investment in seed and early stage businesses or businesses that either do not have established cash flow or that need to use available cash for other purposes.

Legislation is required to address several problems in the SBIC program. In 2004, the participating securities program ceased issuing new leverage commitments. This was largely the result of the Administration's decision to move the program to zero-subsidy in 2001, which was fundamentally unsuited to a program that functioned on patient equity investment in long-term assets. As a result, the program was essentially rendered insolvent by 2005 when the administration requested no program funding for the participating securities portion of the SBIC program in its annual budget request. The Administration continued to pursue these policies in the FY 2008 budget.

By eliminating the participating securities program, however, the SBA has become completely reliant on debt-based programs, which are more suited to providing later stage, expansion capital to cash-flow-positive businesses. This has particularly hampered investment in early-stage and capital-intensive small businesses, which lack the resources to service heavy debt investment. In 2002 the SBA licensed 41 new SBIC funds, more than half of which were for early stage investment. By contrast, in 2006 the SBA licensed only 10 new SBIC funds, none of which were for investment in early stage businesses. These statistics demonstrate the need for some legislative initiative to fill the gap for equitable investment in early stage businesses.

Eliminating participating securities has also had a negative impact on the SBA's ability to provide capital investment for to specific segments of the entrepreneurial community. In FY 2005 only 3.40 percent of all financings in the SBIC program went to small businesses that were majority black owned. Only 1.39 percent of all SBIC investments went to small businesses that were Hispanic owned and only 2.37 percent of SBIC investments went to women

owned businesses. Veteran-Owned small businesses fared the worst, receiving only 0.52 percent of all SBIC financings. While these numbers are better than the 2 percent of equity capital that minority-owned firms receive in the private sector, it still represents a troubling performance for a program that was intended to focus on providing these groups with investment capital.

Additionally, the SBIC program's current leverage limits have proven difficult to apply, particularly when two SBIC funds are under common control. This maximum leverage amount varies depending on the amount of the SBIC's private capital, but generally will not exceed 300 percent of the SBIC's private capital up to $15 million, 200 percent of the amount of private capital between $15 and $30 million, and 100 percent of the amount of private capital between $30 and $75 million. All of these figures are linked to an inflation index and adjust annually. If this program is to have continued success, legislation will be necessary to simplify the leverage cap rules and relax restrictions on the amount of leverage available to SBICs that are under common control.

The New Markets Venture Capital (NMVC) program was established in December of 2000 to address the unmet equity needs of low-income communities. The NMVC program was administered under the purview of the SBA and was modeled after the SBA's Small Business Investment Company (SBIC) program. A crucial difference between NMVC and SBIC, however, was that the NMVC program was established with the specific purpose of providing economic development in low-income (LI) areas.

Like the SBIC program, the NMVC program operates as a public-private partnership between the SBA and licensed New Markets Venture Capital Companies (NMVCCs). The SBA provides funding to NMVCCs, which then use their own funds, plus leverage borrowed with an SBA guaranty, to make investments in smaller enterprises defined by SBA regulations that are located in LI geographic areas. NMVCCs remain privately owned and managed and make their own decisions about which small businesses investments to make.

One crucial advantage that NMVCCs enjoy over SBICs is the addition of SBA administered operational assistance grants (OA). The SBA provides matching grant assistance for the resources that NMVCCs raise to provide marketing, management and other operational assistance to the businesses in which it invests.

In principle, the program was intended to permit NMVC companies to use capital raised with New Markets Tax Credit allocations to meet the NMVC private capital match. In practice, however, this was not possible because the first NMTC allocations were made after NMVC private capital matches were due (e.g. after September 14, 2001) and because the definitions of "low income geographic areas" for the two programs were different. This disparity between the two definitions prevented NMVC companies from using NMTC allocations as matching funds, thus requiring these companies to rely entirely upon privately raised funds for this purpose. Given the economic conditions under which they operate, however, these companies could not find sources of funding. For the program to function as originally intended, the definitions for low income geographic areas must be aligned between the NMTC and NMVC program.

Legislation is also required to achieve the program's initial purpose of providing equity capital to small businesses in LI areas. In 2001 Congress appropriated $150 million of debenture guaranty authority and $30 million for Operational Assistance (OA) grants. Beginning in 2003, however, the administration eliminated funding for the NMVC program. In FY 2008, and consistent with its previous budget request, the administration has not requested any funding for this program. As a result, the SBA has been unable to bring new NMVC companies into the program, limiting access to the program for small businesses in several areas throughout the country.

To date, only six NMVC companies are participating in the program and the FY 2008 budget allocates no resources to bring more companies into the program. If the NMVC program is to meet its full potential to improve economic development in low income communities, legislation must authorize additional appropriations for the program and new initiatives must be established within the program to ensure that the SBA resumes licensing new NMVC companies throughout the nation.

Legislation is also necessary to address the Administration's failure to leverage the program's inherent ability to provide investment capital to industries that have particular difficulty in acquiring equity capital. Historically, no particular style or type of business has attracted NMVC investment. Among existing NMVC Companies, there are multiple fund types and investment styles. These factors reflect a primary benefit of the NMVC program. The additional investment capital provided by the SBA facilitates smaller transactions that are more suitable to investments in smaller businesses and has the added benefit of making NMVC companies less reliant on public market sentiment compared to the investments made by traditional venture capital firms. This is particularly important to facilitating investment in small businesses located in LI areas. As a result, NMVC investments often occur in industries and geographic areas that have historically had difficulty attracting private venture capital. This could provide a particular benefit to LI communities that have experienced a loss of their small manufacturing and industrial economic base.

Despite the success of the SBIC and NMVC programs, the need for early-stage startup capital for small businesses has largely gone unmet by the SBA's existing investment programs, particularly with the elimination of funding for the SBIC Participating Securities program. Additionally, every investment program currently administered by the SBA provides small businesses with debt-based financing, which is more appropriate for investment in later-stage businesses that have the ability to service debt. As a result, legislation is needed to not only fill the gap for early stage business investment, but also provide small businesses with some sort of equity type financing.

Angel investment is a rapidly growing investment strategy that focuses specifically on providing early-stage small business with equity financing. This investment strategy refers to high net worth individuals who invest in and support start-up companies in their early stages of growth. Angels typically invest their own funds, unlike venture capitalists, who manage the pooled money of others in a professionally-managed fund.

Angel investors are often retired business owners or executives, and thus often provide valuable management advice and important contacts to the businesses in which they invest. This commitment of time to mentor and coach entrepreneurs and serve on the boards of portfolio companies is naturally suited to investment in small businesses and mirrors the type of operational assistance often found in SBA programs.

Angel investments typically range from $100,000 to over $1 million dollars. In this respect, angel investors fill the gap that small business start-ups often experience in meeting their needs for equity capital, which are often met with equity raised by friends and family (under $100,000) and funds created by conventional venture capital (VC) firms ($1 million and above). Angel investors will often invest in formal or informal groups, each investor thus contributing about $100,000, thereby limiting their individual risk exposure.

Angels continue to be the largest source of seed and start-up capital, with 46% of 2006 angel investments in the seed and start-up stage. While angels continue to represent the largest source of seed and start-up capital, market conditions and the capital gap in the post seed investing stage are requiring angels to engage in more later-stage investments. New, first sequence, investments represent 63% of 2006 angel activity, indicating that some of this post seed investing is in new deals.

Angel investment has also contributed to a rise of women angel investors and women entrepreneurs. In 2006 women angels represented over 13 percent of the angel market. Women-owned ventures accounted for nearly 13 percent of the entrepreneurs that are seeking angel capital and over 21 percent of these women entrepreneurs received angel investment in 2006. Additionally, minority angels accounted for over three percent of the angel population and minority-owned firms represented nearly 7 percent of the entrepreneurs that presented their business concept to angels.

According to SBA studies, the total unmet need for early-stage equity financing for small businesses is about $60 billion annually. Additionally, partly on the basis of the results of several focus groups that it conducted, the SBA identified that the greatest equity capital financing need of small businesses is financing in the amounts of $250,000 to $5 million. Because of their focus on early stage investing in amounts between $100 thousand to $1 million, angel investing has the potential to make a significant impact on the unmet capital needs of small businesses. These investors, however, are currently poorly organized and may be unaware of the benefits of co-investing with angel groups or angel networks. As a result, legislation is needed to increase public awareness of angel investing, help angel investors to organize into angel groups, and help these groups maintain their focus on investment in startup small businesses. The Committee believes that these goals can be achieved with an Angel Investment Program that focuses on the three traditional strengths of angel investing: providing small business with equity type investment, establishing networks of angel groups and angel investors, and increasing awareness of angel investing.

The SBA has also been limited by the rules that it applies to venture capital companies that invest in small businesses. Venture capital refers to money provided by professionals who invest along-

side management in young, rapidly growing companies that have the potential to develop into significant economic contributors. Venture capital is an important source of equity for start-up companies. Unlike traditional debt-based lenders that secure the amount they lend with collateral, venture firms' investments are backed solely by the strength of the ideas they invest in. A venture capital firm only earns a return on its investment if its investment is highly profitable.

Seeking high-risk investment opportunities because they yield the highest reward, investment firms expect to be able to sell their equity in the business in which they invest within five to ten years. Venture capitalists know that not all their investments will pay-off. The failure rate of investments can be high—anywhere from 20 to 90 percent of the enterprises funded may fail to return the invested capital. As a result, venture capitalists must invest in dozens of small enterprises in the hope that a handful will prove successful.

Under the SBA's current rules, however, all investments made by a single venture capital company are considered affiliated with each other, irrespective of the size of the small business that receives the investment or the size of the venture capital company itself. When added together, the total number of employees often exceeds 500, making each business unable to be defined as a small business concern by SBA. Meeting the requirements of this definition can be the difference for small firms' participation in a wide-variety of government programs, including those involved in cutting-edge defense and health research. The result of this rule is that investment by all but the smallest of venture capital companies is deterred. The common ownership affiliation limitation put forth by the SBA represents a lack of understanding about the venture capital industry practices. The SBA's rule is also inconsistent with industry practices, other SBA programs, and SBA's own statute. For instance, this standard exists even though Small Business Investment Companies, which are themselves venture capital companies, are exempt from such affiliation standards.[1]

In addition, SBA's size standard definition specifies that affiliation occurs when one entity controls or has the power to control another entity.[2] 13 CFR 121.103(c) states that "[a] person that owns, or has power to control, 50 percent more of a concern's voting stock, or block of voting stock which is large compared to other outstanding blocks of voting stock, controls or has the power to control the concern." For most instances, this provision has the effect of deeming venture capital companies to control or have the power to control the concern that they are invested in. This in turn results in the SBA determining that portfolio companies are affiliated with each other through the common affiliation of the venture capital company.

Consequently, legislation is necessary to revise the SBA's application of affiliation rules to small venture capital companies. While venture capital companies invest in multiple business concerns, the affiliation that exists among these portfolio companies is non-existent. Portfolio companies, while receiving investment from the same venture capital company, do not have any common organizational,

[1] 13 CFR 121,103(b)(1).
[2] 13 CFR 121,103(a).

management, or ownership structures. Portfolio companies are separate entities and cannot and do not exercise control over each other. With regard to the venture capital company, portfolio companies receive investment and management assistance, often in the form of director appointments. However, venture capital companies do control portfolio companies that they invest in, rather, they rely on existing management to guide and build the business concerns' profitability. Venture capital companies' ultimate goal is to sell their in the business concern, typically within five to ten years of initial investment.

As a result, the legislation provides that when both the venture capital company and the business receiving investment are small and have less than 500 employees, and when the venture capital company is neither controlled by a large company nor under foreign control, the SBA should not aggregate the whole of the venture capital company's investments for purposes of defining affiliation. In order to allay unfounded fears about the intent of venture capital companies, safeguards have been included to ensure that large companies cannot control venture capital companies, that the venture capital company has less than 500 employees, and is located in the United States.

Legislation is also necessary to strengthen the SBA's Surety Bond Guaranty (SBG) program. The SBG program was established to assist small businesses that would otherwise be able to compete for construction contracts because they failed to meet the criteria necessary to obtain a surety bond. To resolve this problem, the SBG program provides the SBA with authority to guarantee bid, performance, and payment bonds for individual contracts of $2 million or less. In this manner, the SBA provides sureties an incentive to provide bonding for eligible contractors, thereby strengthening contractors' ability to obtain bonding and greater access to contracting opportunities.

The SBA Office of Surety Guarantees (OSG) administers the SBG Program as a public-private partnership between the federal government and the surety industry. The SBG program consists of the Prior Approval program (Plan A) and the Preferred Surety Bond (PSB or Plan B) program.

Under the Plan A, an independent bonding agent reviews the contractor's application package and recommends it to the surety company for approval. If the surety company agrees to issue a bond with the SBA guarantee, the package is forwarded to the appropriate SBA/SBG Area Office and evaluated by SBG personnel. The SBA must approve each bond guarantee individually, based on information submitted by contractor and the surety. If the SBA determines that the applicant is eligible, the SBA issues a bond guarantee to the surety company. The surety then issues the bond to the contractor. The SBA's guarantee agreement is with the surety company, not with the small business contractor. Any surety company certified by the U.S. Treasury to issue bonds may apply for participation in the Prior Approval program.

When Plan A was established, however, many traditional surety companies chose not to participate, often because their business focus was on lower risk, larger contractors, or because the administrative costs of submitting each bond for prior approval of a guar-

anty were significant. To encourage more sureties to participate, the SBA promulgated the Preferred Surety Bond Program (Plan B).

Plan B addressed the concerns of the non-SBA sureties in a number of ways. First, the program provided that if a surety was approved by the SBA for Plan B, it would be granted a dollar value of guaranties from the SBA that would be automatically valid, without prior approval of each bond. In exchange for this reduction of paperwork, however, the sureties would receive only a 70 percent guaranty of loss on each bond rather than the 80 or 90 percent guaranty associated with the Plan A program.

From the perspective of surety companies, the burden associated with the Plan A program has always been justified by the fact that Plan A bonds were reviewed and approved by the SBA prior to the surety issuing the bond. Because of this, Plan A bonds carried the benefits of a speedier guaranty payment in the event that the contract was breached and the bond was executed. Recently, however, many surety companies have complained of the SBA engaging in additional reviews of Plan A bonds to unravel its guaranty after the bond was approved and issued by the surety. This presents a serious problem for sureties because their bond cannot be canceled after having been issued and once the SBA has refused indemnification, sureties bear the entire cost of default.

At the same time that the SBA has faced increasing unpopularity for participation in the Plan A program, Plan B has also become less attractive to surety companies. The primary disincentive for this program has largely been attributed to limitations on the rates that surety companies have been permitted to charge and to the steadily rising cost of fees to participate in the program. With fewer surety companies participating in the SBG program, small businesses have had increasing difficulty finding sources of surety bonds.

As a result, legislation is needed to resolve the disincentives that have steadily driven surety companies from the Plan A and Plan B portions of the program. The SBA's ability to refuse indemnification based upon information that was provided as part of the guaranty application for a Plan A bond should be limited. Additionally, the SBA must have statutory authority to raise premium rates under the Plan B program and reduce the cost of participation fees as necessary.

III. Hearings

In the 110th Congress, the Committee on Small Business held a hearing to examine the SBA's investment programs and the role of venture capital in small business investment on June 21, 2007. The Committee subsequently held a hearing on legislative proposals to address issues raised in the June 21, 2007 hearing and expand small business investment on September 6, 2007.

IV. Committee Consideration

The Committee on Small Business met in open session on September 20, 2007, and ordered H.R. 3567 reported to the House by a voice vote.

V. Committee Votes

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. A motion by Ms. Velázquez to report the bill, without amendment, to the House with a favorable recommendation was AGREED to by voice vote.

VI. Section-by-Section Analysis of H.R. 3567

TITLE I. SBIC PROGRAM

Section 1. Simplified maximum leverage limits

Currently, the leverage caps for SBIC companies vary depending on the amount of the SBIC's private capital, but effectively will not exceed 300 percent of the SBIC's private capital up to $15 million, 200 percent of the amount of private capital between $15 and $30 million, and 100 percent of the amount of private capital between $30 and $75 million. All of these figures are linked to an inflation index and adjust annually.

It is common for SBICs with good records to secure a second or even third SBIC license (supported by new private capital) so that they can continue to operate with uninterrupted investment before winding up all affairs of previous funds and repaying all leverage. The fact that the leverage cap applies to the whole family of funds, however, often makes it impossible for a successful SBIC to operate a second or third fund due to lack of available leverage because of the leverage cap, not because of any increased risk to SBA based on poor financial performance.

This provision is intended to simplify the leverage cap rules to a single formula, regardless of the amount of private capital that the SBIC has, with a maximum leverage cap of $150 million. Additionally, this provision will make "transition" leverage available for SBIC companies under common control so that successful SBICs may operate a second or third fund while still maintaining safeguards against increased risk to the SBA and a maximum leverage cap for SBICs under common control.

These changes are not intended to have retroactive effect. These would be prospective changes only, intended only for SBIC firms licensed in the fiscal year following enactment of this provision. Additionally, these changes are not intended to serve as an entitlement for SBIC firms to receive the maximum leverage limit or to receive multiple licenses. The Committee fully intends for the SBA's to exercise the same discretion as it currently has in deciding the amount of leverage any SBIC firm may receive.

Section 2. Increased investments in women-owned and socially disadvantaged small businesses

Currently, there are no special incentives to encourage SBICs to invest in women-owned and minority-owned small businesses. Additionally, the incentives for investments in low-income areas are confusing and difficult to administer. This section will establish a simple incentive to form funds focused on investment in minority, veteran, and women owned businesses by permitting such funds to operate with increased maximum leverage limits. This section is not intended to displace existing low-and-moderate income deben-

tures or other initiatives aimed at encouraging investment in low income areas, but should be a compliment to these efforts at increasing investment in women, veteran, and minority owned small businesses.

Section 3. Increased investments in smaller enterprises

Currently, SBICs that use of leverage up to $90 million must make no less than 20 percent of its investments in a subset of qualified small businesses defined as "smaller enterprises." SBICs that use more than $90 million in leverage must make 100 percent of its investments with leverage above $90 million in "smaller enterprises." As the leverage cap continues to grow this provision creates record keeping problems and imposes additional "tracking" workloads on the SBA and the affected SBICs.

This provision will simplify the requirements for investment in smaller enterprises and is intended to increase overall investment in smaller enterprises through the SBIC program. This section will establish a flat 25 percent "smaller enterprises" requirement for all SBICs, regardless of whether they have more than $90 million in leverage. This is intended to simplify the administration and increase the percentage of all investments that must be in smaller enterprises.

Section 4. Simplified aggregate investment limitations

The term "Aggregate Limitations" refers to the maximum amount of capital any leveraged SBIC may invest in a single small business or smaller enterprise. The purpose of the limitation is to ensure that leveraged SBICs have diversified portfolios, thus mitigating investment risk for both private investors and the government. Section 306(a) of the Small Business Investment Act of 1958 provides that no leveraged SBIC may make an investment in a small business or smaller enterprise that exceeds an amount equal to 20% of the SBIC's private capital.

This aggregate limitation creates a problem because different leveraged SBICs plan for different ratios of leverage to private capital in their formation process. The projected ratios most often approved in the licensing process are between 1:1 and 2:1 even though the SBIA provides for as much as 3:1 in some cases. The application of a maximum investment amount based on a percentage of private capital versus a percentage of total capital to be managed produces inconsistent results unrelated to risk and prevents many SBICs from supporting small businesses, particularly larger and more well-established small businesses.

This section is intended to revise the current limit on the amount that can be invested in any one portfolio company to standards that are more consistent with industry accepted portfolio risk management practices. This change would apply the portfolio management rule ("no more than 10% should be invested in any one company") that is the accepted norm in the non-SBIC venture capital world and would ensure that SBIC management teams had both the financial and time resources required to help their portfolio companies achieve their growth goals.

It is the Committee's understanding that very few SBIC firms are licensed with business plans to operate with a third tier of leverage, and virtually no firms set forth plans to operate a third tier

in the business plan approved by the Administration at the time the company's license was granted. Consequently, these changes are not intended to have retroactive effect. These would be prospective changes only, intended only for SBIC firms licensed in the fiscal year following enactment of this provision.

TITLE II. NEW MARKETS VENTURE CAPITAL PROGRAM

Section 1. Expansion of new markets venture capital program

To date, only six NMVC companies are participating in the New Markets program and the SBA's FY 2008 budget allocates no resources to bring more companies into the program.

This section is intended to establish mandatory language in the Small Business Investment Act of 1958 directing the SBA Administrator to actively engage in affirmative actions to expand the number of NMVC companies and increase the number of investments made by current and new NMVC companies.

This section would also require the Administrator to perform a study on their success in expanding the NMVC program and report his progress in expanding the program no later than one year after the enactment of this provision.

Section 2. Improved nationwide distribution

Currently, small business investment is concentrated in only a handful of geographic areas, which are primarily located along the East and West coasts of the U.S. This section is intended to direct the SBA Administrator to ensure that there is a uniform distribution of NMVC companies nationwide to the maximum extent possible. In licensing new NMVC companies, this section intends the Administrator to avoid allocating his limited program resources to license new NMVC companies where existing NMVC companies already exist and can meet the demand for small business investment in low income areas.

Section 3. Increased investment in small manufacturers

Many low income communities throughout the nation have suffered as a result of a loss of their small manufacturing and industrial economic base. The NMVC company has an inherent ability to provide investment capital to these communities because the additional investment capital provided by the SBA facilitates smaller transactions that are more suitable to investments in low income communities and makes NMVC companies less reliant on public market sentiment compared to the investments made by traditional venture capital firms. Consequently, NMVC investments can flow to industries like small manufacturing, which has recently suffered particular difficulty in attracting private venture capital.

This section will reduce the capital requirements required for NMVC companies primarily engaged in investment in small manufacturers, making it easier for these companies to secure final approval from the SBA. It is expected that the SBA will facilitate the licensing of these NMVC companies, particularly in low income communities that have lost a significant portion of their small manufacturing industry.

Section 4. Updating definition of low-income geographic area

This section would amend the current definition of "low-income geographic area" by simply referring the definition directly to the definition of a "low-income community" in the Internal Revenue Code.

The Committee believes that the NMVC program's current definition of "low income geographic area" creates a significant barrier to the program's success. As long as the definitions between the NMVC program and the NMTC program are different, NMVC companies will have difficulty in operating in low income communities. This result is inconsistent with the program's original intent.

This section is intended to establish parity between the definitions of the eligible NMVC investments and NMTC allocations, thereby bringing these two programs into alignment. This change will help the program operate as it was originally intended and will permit investment firms to use capital raised with New Markets Tax Credit allocations to meet the program's requirements for matching private capital. Additionally, this approach ensures that the two definitions will remain aligned even in the event that eligibility conditions for tax credit allocations are changed at a future date.

Section 5. Study on availability of equity capital

This Section also requires the Chief Counsel for Advocacy of the SBA to conduct a study on the availability of equity capital in low-income urban and rural areas and report its findings to Congress within 90 days of the study's completion.

Section 6. Expanding operational assistance to conditionally approved companies

This section will permit New Markets Venture Capital Companies that have received conditional approval from the SBA under section 354 to receive early grant assistance up to $50,000 at the point of initial designation. In the event that a conditionally approved NMVC company fails to win final approval, however, the grant must be repaid to the SBA. If the company wins final approval, however, amount of early grant assistance will be deducted from the total amount of operational grant assistance the company receives. Additionally, this section provides NMVC companies with two full years to raise private capital and matching funds for operational assistance. Currently, these companies have up to two years under current law.

These changes are intended to remedy two longstanding problems in the NMVC program. Under existing statutes, NMVC companies could not receive operational assistance grants until after they received final approval. This restriction severely limited the ability of NMVC companies to provide this assistance to their investment concerns, which is often vital to ensuring the success of these businesses and the security of their investment. This change is intended to provide very limited OA grants prior to final approval.

These changes are also intended to remedy the problem that many NMVC companies experienced in reaching final approval. For many NMVC companies, raising the private capital and matching OA funds was the greatest barrier to winning final approval.

By extending the timeframe for matching funds to two full years, these companies should have adequate time to raise private capital that is integral to the NMVC program.

Section 7. Streamlined application for new markets venture capital program

This section will require the SBA to develop a set of documents that reduce the cost and burden for New Markets Venture Capital companies applying for final approval under the program. These documents must be created within 60 days after the enactment of the bill.

This section is intended to simplify the application process for new NMVC companies, enabling the SBA to license more companies and expand the program. This section is also intended to operate in conjunction with the expansion and nationwide distribution initiatives established by this legislation.

Section 8. Elimination of matching requirement

This section will eliminate the minimum amount of matching commitments for operational assistance that an NMVC company must raise before receiving final approval. Currently, this minimum is set at not less than 30 percent of the total amount of private capital or binding capital commitments the NMVC company has raised.

The requirement for matching OA commitments proved to be the greatest barrier to licensing new NMVC companies. The required matching commitments were simply too high for many NMVC companies to meet, particularly given the economic conditions in the communities in which they operate. By eliminating this requirement, this section is intended to enable many more NMVC companies to participate in the program and should streamline the process to winning final approval from the SBA.

Section 9. Simplified formula for operational assistance grants

This section will revise the amount of operational assistance grants a NMVC company may receive. The new amounts will be equal to either 10 percent of the private resources the company has raised for operational assistance, or $1 million, whichever is less.

This section is intended to significantly simplify the formula for determining the amount of OA grants a NMVC company may receive, enabling companies to receive their OA allocations more quickly than they currently do and providing these companies with greater certainty as to the amount of OA resources that they will have.

Section 10. Authorization of appropriations and dedication to small manufacturing

This section reauthorizes appropriations in a total amount of $30 million to fund debenture guarantees and $5 million for operational assistance grants for fiscal years 2008, 2009, and 2010. Additionally, this section requires that at least a quarter of these authorized funds be used for the purpose of entering into participation agreements and providing operational assistance to NMVC companies that invest primarily in small manufacturing business concerns.

This section is intended to reestablish funding for the NMVC companies and, in conjunction with the program expansion and licensing initiatives of this legislation would require the SBA to resume licensing new NMVC companies and providing additional leverage commitments to existing NMVC companies. The initiative for small manufacturing is specifically intended to increase the number of NMVC companies that primarily invest in small manufacturers. This section should not, however, present an additional barrier for NMVC companies that wish to invest in low income areas or that do not wish to invest in small manufacturers.

TITLE III. ANGEL INVESTMENT PROGRAM

Establishment of Angel Investment Program

This legislation will establish an Office of Angel Investment within the Investment Division of the SBA. This office will be headed by a Director of Angel Investment, who will be responsible for administering the Angel Finance Program and Federal Angel Network established by the bill.

As with other SBA programs, the Angel Finance Program will function as a public-private partnership between the SBA and privately organized "angel groups." Angel groups will consist of ten or more accredited investors (as that term is defined under Rule 501 of Regulation D of the Securities and Exchange Act of 1933, 17 C.F.R. Part 230 et seq.). Alternately, an individual may qualify as an angel investor on the basis of such factors as financial sophistication, income, net worth, knowledge, and experience in financial matters, or amount of assets under management. Angel groups should have demonstrated experience in making investments in local small business concerns and must have established protocols for performing due diligence in its investments prior to making investments. Additionally, these angel groups should have an established code of ethics and policies and procedures to avoid conflicts of interest between members of the group and the companies in which they invest.

These angel groups will be licensed by the SBA specifically for the purpose of making investments early stage domestic small business concerns located in the same community as the angel group. In exchange for complying with the program's licensing and investment requirements, angel groups will receive up to $2 million in leverage financing from the SBA that will be co-invested with the angel group's own funds. SBA leverage should only be used to invest in small business concerns that have been in existence for less than 5 years and that have fewer than 75 employees. Additionally, angel groups should not invest SBA leverage abroad, but should use this leverage to invest in local small business concerns that are located within their own community. Finally in selecting angel groups to receive leverage, the SBA should, to the maximum extent possible, avoid licensing new angel groups where a strong angel network already exists and should give priority consideration to angel groups that invest in small businesses owned by veterans, minorities, and women.

Leverage financing that angel groups receive must be invested in a local small business concern with an equal or greater amount of private investment capital raised by the angel group. SBA leverage

should function as a true sidecar investment, and should mirror the private matching investment vehicle. Leverage will be repaid from the pro rata share of any returns on the private matching investment, whether positive or negative, but relative to the amount of leverage that the angel group receives on their investments. Repayment is not premised upon a timeframe, but is instead dependent upon the distribution of any return, whether positive or negative. Additionally, SBA leverage should maintain any preemptive rights in the event that additional ownership interests in the investment enterprise are issued.

As leverage is repaid, amounts collected by the SBA will be deposited in an Angel Investment Fund at the U.S. Treasury. The Angel Investment Fund will serve as a revolving source of leverage financing for the Angel Finance Program to operate without regard to fiscal year limitations.

The legislation will also create Federal Angel Network within the Office of Angel Investment that will collect and maintain information on local and regional angel investors and angel groups. This information will include a list of names and addresses of angel groups and angel investors, information about the types of investments each angel investor or angel group has made, and information on other public and private resources on angel investors and angel groups. This information will be maintained in a regularly updated searchable database available through the SBA's database. Additionally, information contained within the database will be readily available for use and distribution by other angel networks and groups, thereby augmenting the exposure of the Federal Angel Network. Angel investors and angel groups will have the option of excluding their information from the network.

Finally, the Administrator will also carry out a grant program to make grants to entities that develop new or existing angel groups or to increase awareness and education about angel investing. Grant recipients could include units of state or local governments, nonprofit organizations, or Small Business Development Centers or Women Business Centers established under the Small Business Act. To receive grant assistance, however, eligible entities must raise matching funds equal to half of the grant amount, thus strengthening their commitment and amplifying the grant assistance itself. As with SBA leverage, the grants administered under this section are intended to go to entities located in areas where a strong network of angel groups currently does not exist, but where there are sufficient numbers of potential angel investors.

TITLE IV. SURETY BOND PROGRAM

Section 1. Study and report

This section requires that within 180 days of enactment, the Administrator must conduct a study of the program's current funding structure and report its results to Congress. This study should include:

(1) An assessment of whether the program's current funding framework and program fees are retarding the program's growth;

(2) An assessment of whether surety companies and small business concerns could benefit from an alternative funding structure;

(3) An assessment of whether permissible premium rates fore surety companies participating in the program should be placed on parity with the rates authorized by appropriate state insurance regulators and how such a change would affect the program under the current funding framework.

This section is intended to examine the Surety Bond programs current funding structure as a revolving fund program. The findings in this study would serve as the basis for additional legislative action that could reform the funding structure for the program.

Section 2. Preferred surety bond program

This provision will establish explicit statutory authority for a preferred surety bond program that would essentially mirror the preferred lender program under section 7(a) of the Small Business Act. Under the PSB program, the Administrator shall carry out a program under which a written agreement between the surety and the Administration delegates to the surety complete authority to issue, monitor, and service bonds subject to guaranty from the Administration without obtaining the prior specific approval of the Administration. The Administration may recertify PSB sureties for an additional term not to exceed two years. Prior to recertification, the Administration shall review a surety's bonds, policies, and procedures for compliance with relevant rules and regulations. Bonds made under this program shall carry a 70% guaranty.

This section should not make any substantive changes to the existing preferred surety bond program, but is intended to establish more discrete statutory authority for the program that will simplify the process for future revisions or changes to the program.

Section 3. Denial of liability

For bonds made or executed with the Administration's prior approval, the Administration shall not deny liability to a surety based upon information that was provided as part of the guaranty application.

This section is intended to prevent the problem of the SBA denying indemnification for guarantees issued with prior approval from the SBA if the SBA's basis for denying indemnification could have been resolved with a proper review of information contained in the guaranty application.

Section 4. Increasing the bond threshold

This section will increase the maximum permissible bond amount from $2 million to $3 million. This is intended to permit bond companies to issue larger bonds with SBA guarantees, which should encourage greater participation in the program by both small businesses and bond companies.

Section 5. Fees

This section will permit the Administrator to make contributions for the purpose of reducing fees, if and when an appropriation is made available for that purpose. The Committee intends for this provision to make the surety bond program more affordable to

small businesses and surety companies that participate in the program by providing the SBA with authority to contribute funds for the purpose of reducing the burden associated with bonding fees. The Committee does not believe that the stability that the program currently enjoys will be disturbed by this change. The administration will continue to asses and collect the fees necessary to operate the program without and will continue to calculate the budget estimates and assumptions for the fiscal year just as it currently does to operate the program. The Committee foresees no circumstance in which the program would cease operation or be short of necessary program level to operate at full capacity.

This section simply provides the administration with the authority to contribute funds to reduce the fee burden associated bond guarantees if and when an appropriation is made available for that purpose. In years when no appropriation is made available, the Committee expects the program to function with the stability that currently exists. In years when a subsidy is made available, small businesses and surety companies will enjoy the benefits of reduced fee burdens.

TITLE V. VENTURE CAPITAL INVESTMENT

Section 1. Determining whether business concern is independently owned and operated

This section specifies that the SBA shall not consider venture capital investment in determining whether or not a company is defined as a small business. The provision provides that when calculating the number of employees of a small business concern that has venture capital investment, the SBA will exclude those employees who work for companies affiliated with the venture capital company. The bill requires that the venture capital company comply, as appropriate, with federal registration requirements for investment companies. In addition, the bill prevents a venture capital that is controlled by a large business or a venture capital company with more than 500 employees from being recognized as a venture capital company under this provision. The legislation also prevents concerns not located in the United States that control small business concerns to be able to take advantage of this definition.

This section is intended to remove the current disincentive that exists for small businesses to seek and accept venture capital financing. Under the SBA's current rules, all investments made by a single venture capital company are considered affiliated with each other, irrespective of the size of the small business that receives the investment or the size of the venture capital company itself. When added together, the total number of employees often exceeds 500, making each business unable to qualify as a small business concern under the SBA's size standards. Because several federal programs are tied to this qualification, small businesses that receive venture capital financing are frequently disqualified from participating in a wide-variety of government programs that provide substantial benefits to small benefits.

The Committee does not intend for this section to provide a mechanism for large businesses to benefit from small business opportunities, as both the venture capital company and the small

business must themselves qualify as small businesses in their own capacity and cannot be controlled by a large business.

TITLE VI. REGULATIONS

This section requires the SBA to promulgate revisions implementing necessary regulatory changes within 90 days.

VII. Congressional Budget Office Cost Estimate

SEPTEMBER 25, 2007.

Hon. NYDIA M. VELÁZQUEZ,
Chairwoman, Committee on Small Business,
House of Representatives, Washington, DC.

DEAR MADAM CHAIRWOMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 3567, the Small Business Investment Expansion Act of 2007.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susan Willie.

Sincerely,

PETER R. ORSZAG.

Enclosure.

H.R. 3567—Small Business Expansion Act of 2007

Summary: H.R. 3567 would reauthorize the Small Business Administration's (SBA's) New Markets Venture Capital Program (NMVC), amend its surety guarantee program, and change certain investment limits imposed on SBA's small business investment program. The bill also would establish the Angel Investment Program to provide venture capital to certain groups working with small businesses in their communities. Finally, the SBA would be required to produce a number of reports for the Congress about the effectiveness of the program changes authorized by the bill.

Based on information from SBA, CBO estimates that implementing H.R. 3567 would cost $8 million in 2008 and $102 million over the 2008–2012 period, assuming appropriation of the necessary and specified amounts. Enacting H.R. 3567 would not affect direct spending or revenues.

H.R. 3567 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).

Estimated cost to the Federal Government: The estimated budgetary impact of H.R. 3567 is shown in the following table. The costs of this legislation fall within budget function 370 (commerce and housing credit).

	By fiscal year, in millions of dollars—				
	2008	2009	2010	2011	2012
CHANGES IN SPENDING SUBJECT TO APPROPRIATION					
New Markets Venture Capital Program:					
Loan Guarantees:					
Estimated Authorization Level	2	2	2	0	0
Estimated Outlays	1	2	2	1	0
Grants:					
Authorization Level	2	2	1	0	0
Estimated Outlays	0	1	2	1	1

	By fiscal year, in millions of dollars—				
	2008	2009	2010	2011	2012
Angel Investment Program:					
Equity Investments:					
Authorization Level	10	20	20	0	0
Estimated Outlays	2	26	20	2	0
Grants:					
Authorization Level	2	2	2	0	0
Estimated Outlays	0	1	1	1	1
Administrative Cost:					
Authorization Level	1	0	0	0	0
Estimated Outlays	1	0	0	0	0
Surety Bond Fees:					
Estimated Authorization Level	8	8	8	8	8
Estimated Outlays	4	8	8	8	8
Total Changes:					
Estimated Authorization Level	25	34	33	8	8
Estimated Outlays	8	38	33	13	10

Basis of estimate: For this estimate, CBO assumes that the bill will be enacted near the start of fiscal year 2008, that the necessary amounts will be appropriated for each fiscal year, and that spending for programs authorized by the bill will follow historical spending patterns for similar SBA programs.

The budgetary accounting for SBA's direct loan and loan guarantee programs is governed by the Federal Credit Reform Act (FCRA) of 1990, which requires an appropriation of subsidy and administrative costs associated with loan guarantees and loan operations. The subsidy cost is the estimated long-term cost to the government of a loan or loan guarantee, calculated on a net-present-value basis, excluding administrative costs. Administrative costs, recorded on a cash basis, include activities related to making, servicing, and liquidating loans as well as overseeing the performance of lenders.

The effect of the changes that H.R. 3567 would make to SBA's small business investment programs is measured in terms of projected subsidy costs. The bill does not specify an authorization level for either the subsidy or administrative costs, if any, that could be incurred as a result of implementing the amendments in the bill. CBO has estimated those amounts based on information from SBA regarding the historical demand for credit assistance and costs of the agency's small business investment programs. CBO assumes that administrative activities related to those loans would need to continue beyond the 2008–2010 authorization period addressed in this bill.

New Markets Venture Capital Program (NMVC)

The bill would reauthorize the NMVC for three years, through 2010, by authorizing the appropriation of funds sufficient to offer $30 million in loan guarantees and $5 million in technical assistance grants over the three-year period. The bill would direct SBA to approve at least one company from each of SBA's geographic regions to participate in the program, if practicable. H.R. 3567 also would authorize SBA to award technical assistance grants to companies that have received conditional, but not yet final, approval to participate in the program.

Based on information from SBA, CBO expects that the subsidy rate for the NMVC program would be about 17 percent. CBO esti-

mates that reauthorizing the NMVC program would cost $1 million in 2008 and $11 million over the 2008–2012 period, assuming appropriation of the necessary and specified amounts. Of the five-year total, $6 million would be for costs associated with extending loan guarantees; the remaining $5 million would be for costs associated with awarding technical assistance grants.

Angel Investment Program

The bill would authorize a new program to provide equity investments in "angel groups" to provide capital to small businesses located in their communities. As a condition of participation in the program, such groups would be required to repay SBA for any investments that earn a profit. Any amount to be repaid would be prorated based on the share of capital provided by SBA. Repayments would be held by SBA for the purpose of providing new financing to angel groups, subject to provisions in annual appropriation acts. Based on information from SBA, CBO expects that equity investments in angel groups would take several years to generate profits; therefore, a negligible amount of repayments would be collected from such groups over the 2008–2012 period. Moreover, no direct spending savings from such profit-sharing receipts could be credited to this legislation because subsequent appropriation acts would determine the amount and timing of any federal funds made available for the Angel Investment Program.

The bill would establish the Office of Angel Investments within SBA to oversee the Angel Investment Program, to develop a database of information related to angel groups and angel investors, and to award grants to eligible entities to develop new angel groups.

The bill would authorize the appropriation of $13 million in 2008 and $57 million over the 2008–2012 period to carry out the investment, grant, and administrative activities of the program. Based on information from SBA, CBO estimates that implementing the Angel Investment Program would cost $3 million in 2008 and $55 million over the 2008–2012 period, assuming appropriation of the specified amounts.

Surety bond program

The bill would authorize SBA to delegate its authority to issue, monitor, and service surety bonds to entities approved by SBA for such activities. The bill also would eliminate fees that are currently charged to contractors and sureties under the program and authorize the appropriation of sufficient funds to offset the loss of income from fees.

Under current law, SBA's surety bond program provides guarantees to eligible contractors that SBA will reimburse the surety (an entity issuing an assurance that a contractor will perform according to the terms of a signed contract) for a portion of the loss should the contractor breach the terms of the contract. To cover the costs of those guarantees, fees are paid to SBA by both the contractor receiving the guarantee, and the surety that issues the bond for the contractor's performance. In 2006, SBA provided guarantees under the surety bond program for about 5,000 bonded contracts and collected about $7 million in fees. (Those collections are recorded as an offset to discretionary appropriations.) Based on in-

formation from SBA, CBO expects that eliminating the fees paid by participants would lead to a small increase in participation in the program.

Guarantees provided under the surety bond program are recorded as cash expenditures rather than net-present-value costs under FCRA. This is because under the surety bond program, SBA is not guaranteeing repayment under a contract for a loan; rather, it is guaranteeing actual performance under a contract for services, which does not qualify as a loan or loan guarantee under FCRA. CBO estimates that implementing this provision of H.R. 3567 would cost $4 million in 2008 and $36 million over the 2008–2012 period, assuming appropriation of the necessary amounts.

Other provisions

H.R. 3567 would amend provisions of current law that limit the amount of capital SBA can provide to participating small business investment companies (SBICs). Among other things, the bill would change the method for calculating the maximum amount of capital that can be provided to SBICs and raise those limits for SBICs that agree to invest specific amounts in companies owned by individuals from socially or economically disadvantaged or low-income areas, veterans, or members of the National Guard or Reserves. Based on information from SBA, CBO estimates that those changes to the operations of the small business investment program would have an insignificant effect on the federal budget.

The bill also would require SBA to produce four reports for the Congress that assess either the current practices of programs authorized by the bill or the effectiveness of new programs. CBO estimates that the cost of producing those reports would be less than $500,000 per year over the 2008–2012 period.

Intergovernmental and private-sector impact: H.R. 3567 contains no intergovernmental or private-sector mandates as defined in UMRA. The bill would benefit state and local governments by authorizing grants to develop an investment program for small business.

Estimate prepared by: Federal Costs: Susan Willie; Impact on State, Local, and Tribal Governments: Elizabeth Cove; Impact on the Private Sector: Jacob Kuipers.

Estimate approved by: Peter H. Fontaine, Assistant Director for Budget Analysis.

VIII. Committee Estimate of Costs

Clause 3(d)(2) of rule XIII of the Rules of the House of Representatives requires an estimate and a comparison by the Committee of the costs that would be incurred in carrying out H.R. 3567. However, clause 3(d)(3)(B) of that rule provides that this requirement does not apply when the Committee has included in its report a timely submitted cost estimate of the bill prepared by the Director of the Congressional Budget Office under section 402 of the Congressional Budget Act.

IX. Oversight Findings

In accordance with clause (2)(b)(1) of rule X of the Rules of the House of Representatives, the oversight findings and recommenda-

tions of the Committee on Small Business with respect to the subject matter contained in H.R. 3567 are incorporated into the descriptive portions of this report.

X. Statement of Constitutional Authority

Pursuant to clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee finds the authority for this legislation in Article I, Section 8, clause 18, of the Constitution of the United States.

XI. Compliance With Public Law 104–4

H.R. 3567 contains no unfunded mandates.

XII. Congressional Accountability Act

H.R. 3567 does not relate to the terms and conditions of employment or access to public services or accommodations with the meaning of section 102(b)(3) of P.L. 104–1.

XIII. Federal Advisory Committee Statement

This legislation does not establish or authorize the establishment of any new advisory committees.

XIV. Statement of No Earmarks

Pursuant to clause 9 of rule XXI, H.R. 3567 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9(d), 9(e), or 9(f) of rule XXI.

XV. Performance Goals and Objectives

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee establishes the following performance related goals and objectives for this legislation:

H.R. 3567 includes a number of provisions designed to update and improve the Small Business Administration's SBIC, NMVC, and Surety Bond programs, establish a new Angel Investment Program under the purview of the Small Business Administration, and revise existing SBA rules that inhibit venture capital investment in small businesses.

Changes in Existing Law Made by the Bill, as Reported

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

SMALL BUSINESS INVESTMENT ACT OF 1958

* * * * * * *

TITLE III—INVESTMENT DIVISION PROGRAMS

PART A—SMALL BUSINESS INVESTMENT COMPANIES

* * * * * * *

BORROWING POWER

SEC. 303. (a) * * *

(b) To encourage the formation and growth of small business investment companies the Administration is authorized when authorized in appropriation Acts, to purchase, or to guarantee the timely payment of all principal and interest as scheduled on, debentures or participating securities issued by such companies. Such purchases or guarantees may be made by the Administration on such terms and conditions as it deems appropriate, pursuant to regulations issued by the Administration. The full faith and credit of the United States is pledged to the payment of all amounts which may be required to be paid under any guarantee under this subsection. Debentures purchased or guaranteed by the Administration under this subsection shall be subordinate to any other debenture bonds, promissory notes, or other debts and obligations of such companies, unless the Administration in its exercise of reasonable investment prudence and in considering the financial soundness of such company determines otherwise. Such debentures may be issued for a term of not to exceed fifteen years and shall bear interest at a rate not less than a rate determined by the Secretary of the Treasury taking into consideration the current average market yield on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the average maturities on such debentures, adjusted to the nearest one-eighth of 1 per centum, plus, for debentures obligated after September 30, 2001, an additional charge, in an amount established annually by the Administration, as necessary to reduce to zero the cost (as defined in section 502 of the Federal Credit Reform Act of 1990 (2 U.S.C. 661a)) to the Administration of purchasing and guaranteeing debentures under this Act, which amount may not exceed 1.38 percent per year, and which shall be paid to and retained by the Administration. The debentures or participating securities shall also contain such other terms as the Administration may fix, and shall be subject to the following restrictions and limitations:

(1) * * *

[(2) MAXIMUM LEVERAGE.—

[(A) IN GENERAL.—After March 31, 1993, the maximum amount of outstanding leverage made available to a company licensed under section 301(c) of this Act shall be determined by the amount of such company's private capital—

[(i) if the company has private capital of not more than $15,000,000, the total amount of leverage shall not exceed 300 percent of private capital;

[(ii) if the company has private capital of more than $15,000,000 but not more than $30,000,000, the total amount of leverage shall not exceed $45,000,000 plus 200 percent of the amount of private capital over $15,000,000; and

[(iii) if the company has private capital of more than $30,000,000, the total amount of leverage shall not exceed $75,000,000 plus 100 percent of the amount of private capital over $30,000,000 but not to exceed an additional $15,000,000.

[(B) ADJUSTMENTS.—

[(i) IN GENERAL.—The dollar amounts in clauses (i), (ii), and (iii) of subparagraph (A) shall be adjusted annually to reflect increases in the Consumer Price Index established by the Bureau of Labor Statistics of the Department of Labor.

[(ii) INITIAL ADJUSTMENTS.—The initial adjustments made under this subparagraph after the date of the enactment of the Small Business Reauthorization Act of 1937 shall reflect only increases from March 31, 1993.

[(C) INVESTMENTS IN LOW-INCOME GEOGRAPHIC AREAS.—In calculating the outstanding leverage of a company for the purposes of subparagraph (A), the Administrator shall not include the amount of the cost basis of any equity investment made by the company in a smaller enterprise located in a low-income geographic area (as defined in section 351), to the extent that the total of such amounts does not exceed 50 percent of the company's private capital.]

(2) MAXIMUM LEVERAGE.—

(A) IN GENERAL.—The maximum amount of outstanding leverage made available to any one company licensed under section 301(c) of this Act may not exceed the lesser of—

(i) 300 percent of such company's private capital; or

(ii) $150,000,000.

(B) MULTIPLE LICENSES UNDER COMMON CONTROL.—The maximum amount of outstanding leverage made available to two or more companies licensed under section 301(c) of this Act that are commonly controlled (as determined by the Administrator) and not under capital impairment may not exceed $225,000,000.

(C) INCREASED INVESTMENTS IN WOMEN-OWNED AND SOCIALLY DISADVANTAGED SMALL BUSINESSES.—The limits provided in subparagraphs (A)(ii) and (B) shall be $175,000,000 and $250,000,000, respectively, for any company that certifies in writing that not less than 50 percent of the company's aggregate dollar amount of investments will be made in small businesses that prior to the investment are—

(i) majority owned by one or more—

(I) socially or economically disadvantaged individuals (as defined by Administrator);

(II) veterans of the Armed Forces; or

(III) current or former members of the National Guard or Reserve; or

(ii) located in a low-income geographic area (as defined in section 351).

* * * * * * *

[(4) MAXIMUM AGGREGATE AMOUNT OF LEVERAGE.—

[(A) IN GENERAL.—Except as provided in subparagraph (B), the aggregate amount of outstanding leverage issued to any company or companies that are commonly controlled (as determined by the Administrator) may not exceed $90,000,000, as adjusted annually for increases in the Consumer Price Index.

[(B) EXCEPTIONS.—The Administrator may, on a case-by-case basis—

[(i) approve an amount of leverage that exceeds the amount described in subparagraph (A) for companies under common control; and

[(ii) impose such additional terms and conditions as the Administrator determines to be appropriate to minimize the risk of loss to the Administration in the event of default.

[(C) APPLICABILITY OF OTHER PROVISIONS.—Any leverage that is issued to a company or companies commonly controlled in an amount that exceeds $90,000,000, whether as a result of an increase in the Consumer Price Index or a decision of the Administrator, is subject to subsection (d).

[(D) INVESTMENTS IN LOW-INCOME GEOGRAPHIC AREAS.—In calculating the aggregate outstanding leverage of a company for the purposes of subparagraph (A), the Administrator shall not include the amount of the cost basis of any equity investment made by the company in a smaller enterprise located in a low-income geographic area (as defined in section 351), to the extent that the total of such amounts does not exceed 50 percent of the company's private capital.]

* * * * * * *

[(d) REQUIRED CERTIFICATIONS.—

[(1) IN GENERAL.—The Administrator shall require each licensee, as a condition of approval of an application for leverage, to certify in writing—

[(A) for licensees with leverage less than or equal to $90,000,000, that not less than 20 percent of the licensee's aggregate dollar amount of financings will be provided to smaller enterprises; and

[(B) for licensees with leverage in excess of $90,000,000, that, in addition to satisfying the requirements of subparagraph (A), 100 percent of the licensee's aggregate dollar amount of financings made in whole or in part with leverage in excess of $90,000,000 will be provided to smaller enterprises (as defined in section 103(12)).

[(2) MULTIPLE LICENSEES.—Multiple licensees under common control (as determined by the Administrator) shall be considered to be a single licensee for purposes of determining both the applicability of and compliance with the investment percentage requirements of this subsection.]

(d) INCREASED INVESTMENTS IN SMALLER ENTERPRISES.—The Administrator shall require each licensee, as a condition of an application for leverage, to certify in writing that not less than 25 percent of the licensee's aggregate dollar amount of financings will be provided to smaller enterprises (as defined in section 103(12)).

* * * * * * *

AGGREGATE LIMITATIONS

SEC. 306. [(a) If any small business investment company has obtained financing from the Administration and such financing remains outstanding, the aggregate amount of obligations and securi-

ties acquired and for which commitments may be issued by such company under the provisions of this title for any single enterprise shall not exceed 20 per centum of the private capital of such company, without the approval of the Administration.]

(a) If any small business investment company has obtained financing from the Administration and such financing remains outstanding, the aggregate amount of securities acquired and for which commitments may be issued by such company under the provisions of this title for any single enterprise shall not, without the approval of the Administration, exceed 10 percent of the sum of—

(1) the private capital of such company; and

(2) the total amount of leverage projected by the company in the company's business plan that was approved by the Administration at the time of the grant of the company's license.

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PART B—NEW MARKETS VENTURE CAPITAL PROGRAM

SEC. 351. DEFINITIONS.

In this part, the following definitions apply:

(1) * * *

[(2) LOW-INCOME INDIVIDUAL.—The term "low-income individual" means an individual whose income (adjusted for family size) does not exceed—

[(A) for metropolitan areas, 80 percent of the area median income; and

[(B) for nonmetropolitan areas, the greater of—

[(i) 80 percent of the area median income; or

[(ii) 80 percent of the statewide nonmetropolitan area median income.

[(3) LOW-INCOME GEOGRAPHIC AREA.—the term "low-income geographic area" means—

[(A) any population census tract (or in the case of an area that is not tracted for population census tracts, the equivalent county division, as defined by the Bureau of the Census of the Department of Commerce for purposes of defining poverty areas), if—

[(i) the poverty rate for that census tract is not less than 20 percent;

[(ii) in the case of a tract—

[(I) that is located within a metropolitan area, 50 percent or more of the households in that census tract have an income equal to less than 60 percent of the area median gross income; or

[(II) that is not located within a metropolitan area, the median household income for such tract does not exceed 80 percent of the statewide median household income; or

[(iii) as determined by the Administrator based on objective criteria, a substantial population of low-income individuals reside, an inadequate access to investment capital exists, or other indications of economic distress exist in that census tract; or

[(B) any area located within—

[(i) a HUBZone (as defined in section 3(p) of the Small Business Act and the implementing regulations issued under that section);

[(ii) an urban empowerment zone or urban enterprise community (as designated by the Secretary of Housing and Urban Development); or

[(iii) a rural empowerment zone or rural enterprise community (as designated by the Secretary of Agriculture).]

(2) LOW-INCOME GEOGRAPHIC AREA.—The term "low-income geographic area" has the same meaning given the term "low-income community" in section 45D(e) of the Internal Revenue Code of 1986 (26 U.S.C. 45D(e)).

[(4)] *(3)* NEW MARKETS VENTURE CAPITAL COMPANY.—The term "New Markets Venture Capital company" means a company that—

(A) * * *

* * * * * * *

[(5)] *(4)* OPERATIONAL ASSISTANCE.—The term "operational assistance" means management, marketing, and other technical assistance that assists a small business concern with business development.

[(6)] *(5)* PARTICIPATION AGREEMENT.—The term "participation agreement" means an agreement, between the Administrator and a company granted final approval under section 354(e), that—

(A) * * *

* * * * * * *

[(7)] *(6)* SPECIALIZED SMALL BUSINESS INVESTMENT COMPANY.—The term "specialized small business investment company" means any small business investment company that—

(A) * * *

* * * * * * *

[(8)] *(7)* STATE.—The term "State" means such of the several States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, Guam, American Samoa, the Commonwealth of the Northern Mariana Islands, and any other commonwealth, territory, or possession of the United States.

* * * * * * *

SEC. 353. ESTABLISHMENT.

In accordance with this part, the Administrator shall establish a New Markets Venture Capital Program, under which the Administrator [may] *shall*—

(1) * * *

* * * * * * *

SEC. 354. SELECTION OF NEW MARKETS VENTURE CAPITAL COMPANIES.

(a) * * *

* * * * * * *

(d) REQUIREMENTS TO BE MET FOR FINAL APPROVAL.—The Administrator shall grant each conditionally approved company [a pe-

riod of time, not to exceed 2 years,] *2 years* to satisfy the following requirements:

(1) CAPITAL REQUIREMENT.—[Each]

(A) IN GENERAL.—Except as provided in subparagraph (B), each conditionally approved company shall raise not less than $5,000,000 of private capital or binding capital commitments from one or more investors (other than agencies or departments of the Federal Government) who met criteria established by the Administrator.

(B) SMALL MANUFACTURER INVESTMENT CAPITAL REQUIREMENTS.—Each conditionally approved company engaged primarily in development of and investment in small manufacturers shall raise not less than $3,000,000 of private capital or binding capital commitments from one or more investors (other than agencies or departments of the Federal Government) who meet criteria established by the Administrator.

(2) NONADMINISTRATION RESOURCES FOR OPERATIONAL ASSISTANCE.—

(A) IN GENERAL.—In order to provide operational assistance to smaller enterprises expected to be financed by the company, each conditionally approved company—

(i) shall have binding commitments (for contribution in cash or in kind)—

(I) from any sources other than the Small Business Administration that meet criteria established by the Administrator; *and*

(II) payable or available over a multiyear period acceptable to the Administrator (not to exceed 10 years); [and]

[(III) in an amount not less than 30 percent of the total amount of capital and commitments raised under paragraph (1);]

* * * * * * *

(f) GEOGRAPHIC EXPANSION.—From among companies submitting applications under subsection (b), the Administrator shall consider the selection criteria and nationwide distribution under subsection (c) and shall, to the maximum extent practicable, approve at least one company from each geographic region of the Small Business Administration.

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SEC. 358. OPERATIONAL ASSISTANCE GRANTS.

(a) IN GENERAL.—

(1) * * *

* * * * * * *

(4) GRANT AMOUNT.—

(A) NEW MARKETS VENTURE CAPITAL COMPANIES.—The amount of a grant made under this subsection to a New Markets Venture Capital company [shall be equal to the resources (in cash or in kind) raised by the company under section 354(d)(2).] *shall be equal to the lesser of—*

(i) 10 percent of the resources (in cash or in kind) raised by the company under section 354(d)(2); or

(ii) $1,000,000.

* * * * * * *

(6) GRANTS TO CONDITIONALLY APPROVED COMPANIES.—

(A) IN GENERAL.—Subject to subparagraphs (A) and (B), upon the request of a company conditionally-approved under section 354(c), the Administrator shall make a grant to the company under this subsection.

(B) REPAYMENT BY COMPANIES NOT APPROVED.—If a company receives a grant under paragraph (6) and does not enter into a participation agreement for final approval, the company shall repay the amount of the grant to the Administrator.

(C) DEDUCTION FROM GRANT TO APPROVED COMPANY.—If a company receives a grant under paragraph (6) and receives final approval under section 354(e), the Administrator shall deduct the amount of the grant under that paragraph from the total grant amount that the company receives for operational assistance.

(D) AMOUNT OF GRANT.—No company may receive a grant of more than $50,000 under this paragraph.

* * * * * * *

SEC. 368. AUTHORIZATIONS OF APPROPRIATIONS.

(a) IN GENERAL.—There are authorized to be appropriated for **[**fiscal years 2001 through 2006**]** *fiscal years 2008 through 2010*, to remain available until expended, the following sums:

(1) Such subsidy budget authority as may be necessary to guarantee **[**$150,000,000**]** *$30,000,000* of debentures under this part*, of which not less than one-quarter shall be used to guarantee debentures of companies engaged primarily in development of and investment in small manufacturers*.

(2) **[**$30,000,000**]** *$5,000,000* to make grants under this part*, of which not less than one-quarter shall be used to make grants to companies engaged primarily in development of and investment in small manufacturers*.

PART C—ANGEL INVESTMENT PROGRAM

SEC. 380. OFFICE OF ANGEL INVESTMENT.

(a) ESTABLISHMENT.—There is established, in the Investment Division of the Small Business Administration, the Office of Angel Investment.

(b) DIRECTOR.—The head of the Office of Angel Investment is the Director of Angel Investment.

(c) DUTIES.—Subject to the direction of the Secretary, the Director shall perform the following functions:

(1) Provide support for the development of angel investment opportunities for small business concerns.

(2) Administer the Angel Investment Program under section 382 of this Act.

(3) Administer the Federal Angel Network under section 383 of this Act.

(4) Administer the grant program for the development of angel groups under section 384 of this Act.

(5) Perform such other duties consistent with this section as the Administrator shall prescribe.

SEC. 381. DEFINITIONS.

In this part:

(1) The term "angel group" means 10 or more angel investors organized for the purpose of making investments in local or regional small business concerns that—

(A) consists primarily of angel investors;

(B) requires angel investors to be accredited investors; and

(C) actively involves the angel investors in evaluating and making decisions about making investments.

(2) The term "angel investor" means an individual who—

(A) qualifies as an accredited investor (as that term is defined under Rule 501 of Regulation D of the Securities and Exchange Commission (17 C.F.R. 230.501));

(B) provides capital to or makes investments in a small business concern.

(3) The term "small business concern owned and controlled by veterans" has the meaning given that term under section 3(q)(3) of the Small Business Act (15 U.S.C. 632(q)(3)).

(4) The term "small business concern owned and controlled by women" has the meaning given that term under section 8(d)(3)(D) of such Act (15 U.S.C. 637(d)(3)(D)).

(5) The term "socially and economically disadvantaged small business concern" has the meaning given that term under section 8(a)(4)(A) of such Act (15 U.S.C. 637(a)(4)(A)).

SEC. 382. ANGEL INVESTMENT PROGRAM.

(a) IN GENERAL.—The Director of Angel Investment shall establish and carry out a program, to be known as the Angel Investment Program, to provide financing to approved angel groups for the purpose of providing venture capital investment in small businesses in their communities.

(b) ELIGIBILITY.—To be eligible to receive financing under this section, an angel group shall—

(1) have demonstrated experience making investments in local or regional small business concerns;

(2) have established protocols and a due diligence process for determining its investment strategy;

(3) have an established code of ethics; and

(4) submit an application to the Director of Angel Investment at such time and containing such information and assurances as the Director may require.

(c) USE OF FUNDS.—An angel group that receives financing under this section shall use the amounts received to make investments in small business concerns—

(1) that have been in existence for less than 5 years as of the date on which the investment is made;

(2) that have fewer than 75 employees as of the date on which the investment is made;

(3) more than 50 percent of the employees of which perform substantially all of their services in the United States as of the date on which the investment is made; and

(4) within the geographic area determined by the Director under subsection (e).

(d) LIMITATION ON AMOUNT.—No angel group receiving financing under this section shall receive more than $2,000,000.

(e) LIMITATION ON GEOGRAPHIC AREA.—For each angel group receiving financing under this section, the Director shall determine the geographic area in which a small business concern must be located to receive an investment from that angel group.

(f) PRIORITY IN PROVIDING FINANCING.—In providing financing under this section, the Director shall give priority to angel groups that invest in small business concerns owned and controlled by veterans, small business concerns owned and controlled by women, and socially and economically disadvantaged small business concerns.

(g) NATIONWIDE DISTRIBUTION OF FINANCING.—In providing financing under this section, the Director shall, to the extent practicable, provide financing to angel groups that are located in a variety of geographic areas.

(h) MATCHING REQUIREMENT.—As a condition of receiving financing under this section, the Director shall require that for each small business concern in which the angel group receiving such financing invests, the angel group shall invest an amount that is equal to or greater than the amount of financing received under this section from a source other than the Federal Government that is equal to the amount of the financing provided under this section that the angel group invests in that small business concern.

(i) REPAYMENT OF FINANCING.—As a condition of receiving financing under this section, the Director shall require an angel group to repay the Director for any investment on which the angel group makes a profit an amount equal to the percentage of the returns that is equal to the percentage of the total amount invested by the angel group that consisted of financing received under this section.

(j) ANGEL INVESTMENT FUND.—

(1) ESTABLISHMENT.—There is in the Treasury a fund to be known as the Angel Investment Fund.

(2) DEPOSIT OF CERTAIN AMOUNTS.—Amounts collected under subsection (i) shall be deposited in the fund.

(3) USE OF DEPOSITS.—Deposits in the fund shall be available for the purpose of providing financing under this section in the amounts specified in annual appropriation laws without regard to fiscal year limitations.

(k) AUTHORIZATION OF APPROPRIATIONS.—There is authorized to be appropriated to carry out this section—

(1) $10,000,000 for fiscal year 2008;

(2) $20,000,000 for fiscal year 2009; and

(3) $20,000,000 for fiscal year 2010.

SEC. 383. FEDERAL ANGEL NETWORK.

(a) IN GENERAL.—Subject to the succeeding provisions of this subsection, the Director of the Office of Angel Investment shall establish and maintain a searchable database, to be known as the Federal Angel Network, to assist small business concerns in identifying angel investors.

(b) NETWORK CONTENTS.—The Federal Angel Network shall include—

(1) a list of the names and addresses of angel groups and angel investors;

(2) information about the types of investments each angel group or angel investor has made; and

(3) information about other public and private resources and registries that provide information about angel groups or angel investors.

(c) COLLECTION OF INFORMATION.—

(1) IN GENERAL.—The Director shall collect the information to be contained in the Federal Angel Network and shall ensure that such information is updated regularly.

(2) REQUEST FOR EXCLUSION OF INFORMATION.—The Director shall not include such information concerning an angel investor if that investor contacts the Director to request that such information be excluded from the Network.

(d) AVAILABILITY.—The Director shall make the Federal Angel Network available on the Internet website of the Administration and shall do so in a manner that permits others to download, distribute, and use the information contained in the Federal Angel Network.

(e) AUTHORIZATION OF APPROPRIATIONS.—There is authorized to be appropriated to carry out this section $1,000,000, to remain available until expended.

SEC. 384. GRANT PROGRAM FOR DEVELOPMENT OF ANGEL GROUPS.

(a) IN GENERAL.—The Director of the Office of Angel Investment shall establish and carry out a grant program to make grants to eligible entities for the development of new or existing angel groups and to increase awareness and education about angel investing.

(b) ELIGIBLE ENTITIES.—In this section, the term "eligible entity" means—

(1) a State or unit of local government;

(2) a nonprofit organization;

(3) a state mutual benefit corporation;

(4) a Small Business Development Center established pursuant to section 21 of the Small Business Act (15 U.S.C. 648); or

(5) a women's business center established pursuant to section 29 of the Small Business Act (15 U.S.C. 656).

(c) MATCHING REQUIREMENT.—The Administrator shall require, as a condition of any grant made under this section, that the eligible entity receiving the grant provide from resources (in cash or in kind), other than those provided by the Administrator or any other Federal source, a matching contribution equal to 50 percent of the amount of the grant.

(d) APPLICATION.—To receive a grant under this section, an eligible entity shall submit an application that contains—

(1) a proposal describing how the grant would be used; and

(2) any other information or assurances as the Director may require.

(e) REPORT.—Not later than 3 years after the date on which an eligible entity receives a grant under this section, such eligible entity shall submit a report to the Administrator describing the use of grant funds and evaluating the success of the angel group developed using the grant funds.

(f) AUTHORIZATION OF APPROPRIATIONS.—There is authorized to be appropriated to carry out this section $1,500,000, for each of fiscal years 2008 through 2010.

TITLE IV—GUARANTEES

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PART B—SURETY BOND GUARANTEES

* * * * * * *

AUTHORITY OF THE ADMINISTRATION

SEC. 411. (a)(1) The Administration may, upon such terms and conditions as it may prescribe, guarantee and enter into commitments to guarantee any surety against loss resulting from a breach of the terms of a bid bond, payment bond, performance bond, or bonds ancillary thereto, by a principal on any total work order or contract amount at the time of bond execution that does not exceed **[**$2,000,000**]** *$3,000,000*.

* * * * * * *

[(3) The Administration may authorize any surety, without further administration approval, to issue, monitor, and service such bonds subject to the Administration's guarantee.

[(4) No such guarantee may be issued, unless—

[(A) the person who would be principal under the bond is a small business concern;

[(B) the bond is required in order for such person to bid on a contract, or to serve as a prime contractor or subcontractor thereon;

[(C) such person is not able to obtain such bond on reasonable terms and conditions without a guarantee under this section; and

[(D) there is a reasonable expectation that such principal will perform the covenants and conditions of the contract with respect to which such bond is required, and the terms and conditions of such bond are reasonable in the light of the risks involved and the extent of the surety's participation.

[(5)(A) The Administration shall promptly act upon an application from a surety to participate in the Preferred Surety Bond Guarantee Program, authorized by paragraph (3), in accordance with criteria and procedures established in regulations pursuant to subsection (d).

[(B) The Administration is authorized to reduce the allotment of bond guarantee authority or terminate the participation of a surety in the Preferred Surety Program Guarantee Program based on the rate of participation of such surety during the 4 most recent fiscal year quarters compared to the median rate of participation by the other sureties in the program.**]**

(b) Subject to the provisions of this section, in connection with the issuance by the Administration of a guarantee to a surety as provided by subsection (a), the Administration may agree to indemnify such surety against a loss sustained by such surety in avoiding or attempting to avoid a breach of the terms of a bond guaranteed by the Administration pursuant to subsection (a): *Provided, however*

(1) * * *

(2) a surety must obtain approval from the Administration prior to making any payments pursuant to this subsection un-

less the surety is participating under [the authority of subsection (a)(3)] *the authority of section 413*; and

* * * * * * *

(c) Any guarantee or agreement to indemnify under this section shall obligate the Administration to pay to the surety a sum—

[(1) not to exceed 70 per centum of the loss incurred and paid by a surety authorized to issue bonds subject to the Administration's guarantee under subsection (a)(3);]

[(2)] *(1)* not to exceed 90 per centum of the loss incurred and paid in the case of a surety requiring the Administration's specific approval for the issuance of such bond, but in no event may the Administration make any duplicate payment pursuant to subsection (b) or any other subsection;

[(3)] *(2)* equal to 90 per centum of the loss incurred and paid in the case of a surety requiring the administration's specific approval for the issuance of a bond, if—

(A) * * *

* * * * * * *

[(4)] *(3)* determined pursuant to subsection (b), if applicable.

* * * * * * *

(g)(1) * * *

* * * * * * *

(3) Each surety participating under [the authority of paragraph (3) of subsection (a)] *the authority of section 413* shall be audited at least once every three years by examiners selected and approved by the Administration.

* * * * * * *

(k) For bonds made or executed with the prior approval of the Administration, the Administration shall not deny liability to a surety based upon information that was provided as part of the guaranty application.

(l) To the extent that amounts are made available to the Administrator for the purpose of fee contributions, the Administrator shall use such funds to offset fees established and assessed under this section. Each fee contribution shall be effective for one fiscal quarter and shall be adjusted as necessary to ensure that amounts made available are fully used.

SEC. 413. PREFERRED SURETY BOND PROGRAM.

(a) PROGRAM REQUIRED.—The Administrator shall carry out a program, to be known as the Preferred Surety Bond Program, under which the Administration, by a written agreement between the surety and the Administration, delegates to the surety complete authority to issue, monitor, and service bonds subject to guaranty from the Administration without obtaining the specific approval of the Administration. Bonds made under the program shall carry a 70 percent guaranty.

(b) TERM.—The term of a delegation of authority under such an agreement shall not exceed 2 years.

(c) RENEWAL.—Such an agreement may be renewed one or more times, each such renewal providing one additional term. Before each renewal, the Administrator shall review the surety's bonds, policies, and procedures for compliance with relevant rules and regulations.

(d) APPLICATION.—The Administrator shall promptly act upon an application from a surety to participate in the program, in accordance with criteria and procedures established in regulations pursuant to section 411(d).

(e) REDUCTION OR TERMINATION OF PARTICIPATION.—The Administrator is authorized to reduce the allotment of bond guarantee authority or terminate the participation of a surety in the program based on the rate of participation of such surety during the 4 most recent fiscal year quarters compared to the median rate of participation by the other sureties in the program.

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SMALL BUSINESS ACT

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SEC. 3. (a)(1) * * *

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(5) NON-AFFILIATION OF VENTURE CAPITAL FROM CONSIDERATION OF SMALL BUSINESS CONCERN.—For purposes of determining whether a small business concern is independently owned and operated under paragraph (1) or meets the small business size standards instituted under paragraph (2), the Administrator shall not consider a concern that has received financing from a venture capital operating company to be affiliated with either the venture capital operating company or any other business which the venture capital operating company has financed.

(6) DEFINITION OF "INDEPENDENTLY OWNED AND OPERATED".—For purposes of this section, a business concern shall be deemed to be "independently owned and operated" if it is owned in majority part by one or more natural persons or venture capital operating companies meeting the definition in paragraph (7).

(7) DEFINITION OF "VENTURE CAPITAL OPERATING COMPANY".—For purposes of this section, the term "venture capital operating company" means a business concern—

(A) that—

(i) is a Venture Capital Operating Company, as that term is defined in regulations promulgated by the Secretary of Labor; or

(ii) is an entity that—

(I) is registered under the Investment Company Act of 1940 (15 U.S.C. 80a–51 et seq.);

(II) is an investment company, as defined in section 3(c)(14) of such Act (15 U.S.C. 80a–3(c)(14)), which is not registered under such Act because it is beneficially owned by less than 100 persons; or

(III) is a nonprofit organization affiliated with, or serving as a patent and licensing organization for, a university or other institution of higher education and that invests primarily in small business concerns; and

(B) that is not controlled by any business concern that is not a small business concern within the meaning of section 3; and

(C) that has fewer than 500 employees; and

(D) that is itself a business concern incorporated and domiciled in the United States, or is controlled by a business concern that is incorporated and domiciled in the United States.

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