

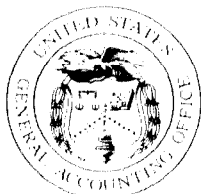
GAO

Report to the Honorable  
Marty Russo, House of Representatives

July 1991

# SMALL BUSINESS

## Evaluation of Investment Companies' Financing Activities



144430

---

---



United States  
General Accounting Office  
Washington, D.C. 20548

---

**Resources, Community, and  
Economic Development Division**

B-244222

July 23, 1991

The Honorable Marty Russo  
House of Representatives

Dear Mr. Russo:

You requested that we review the financing activities of investment companies participating in the Small Business Administration's (SBA) Small Business Investment Company (SBIC) Program. As agreed with your office, this briefing report provides the final results of the analysis that we briefed you on earlier. Specifically, we are providing information on (1) the number and dollar amount of financings<sup>1</sup> made by SBICs and specialized SBICs (SSBIC) in calendar years 1983 through 1989, (2) the size of businesses receiving financing and the purpose of the financing, (3) SBA's definition of "small business concern" and the ability of businesses with large gross assets to qualify for financing, and (4) the role of banks in providing financing through the SBIC and SSBIC programs. Additionally, because of concerns about the financial health of the SBIC Program, we are currently examining the causes of recent investment company liquidations and plan to examine the viability of the SBIC Program in providing venture capital to small businesses.

The Small Business Investment Act of 1958 created the SBIC Program to help small businesses obtain equity capital, management assistance, and long-term financing. The act also established the SSBIC Program, which targets similar assistance to small business concerns owned by socially or economically disadvantaged persons. In return for pledging to finance only small businesses, SBICs and SSBICs qualify for long-term, government-guaranteed debt instruments to augment their own financial resources. SBA's Investment Division administers the SBIC and SSBIC programs, licenses the investment companies, and maintains regulatory oversight over them. As of March 1, 1991, there were 236 active SBICs and 132 active SSBICs.

In summary, our analysis of SBA's data bases on investment companies' financing activities shows the following concerning SBIC and SSBIC financing (see app. I for our assessment of the reliability of SBA's data bases):

---

<sup>1</sup>A financing may be a loan or a debt or equity security.

- Between 1983 and 1989, SBICs and SSBICs made 26,747 financings to small businesses totaling \$4.3 billion. The median size of individual financings was \$66,000. While the annual number of financings increased from 3,308 in 1983 to a peak of 4,308 in 1985, it has declined each year since 1985 to 3,162 in 1989. The total funds invested annually in small businesses generally increased each year from \$488 million in 1983 to \$653 million in 1989. (See sec. 1.)
- Information on the size of the businesses being financed was available for about half of all financings. Most of these financings went to businesses that had less than \$1 million in total assets, less than \$1 million in gross revenues, and fewer than 20 employees. Financings in larger businesses were made almost exclusively by SBICs. Sixty-six percent of all financings were for operating capital. However, financings in businesses with assets of \$10 million or more were twice as likely to be used for acquiring an existing business. (See sec. 2.)
- SBA's current definition of a small business concern does not restrict financing on the basis of asset size. Under SBA regulations, a small business is one that either has a net worth of \$6 million or less and an annual average net income for the preceding 2 years of \$2 million or less, or meets size standards used for other SBA programs. These size standards vary depending on the industry in which the business is primarily engaged and, with few exceptions, rely on measures of annual receipts and number of employees. In recognition of concerns that businesses were receiving SBIC financing for leveraged buy-outs of companies with large assets, SBA proposed regulations in September 1990 that would limit to \$20 million the gross assets of a concern whose change of ownership is financed by an SBIC. This restriction would not apply to SBIC financing for other purposes. As late as September 1979, SBA's size standards for all SBIC financings included a \$9-million asset limit. (See sec. 3.)
- Banks play a significant role in the investment company program. Financings made by SBICs and SSBICs in which banks have at least a 50-percent ownership (called "bank-dominated") totaled \$1.8 billion, or 41 percent of funds provided between 1983 and 1989. While bank-dominated investment companies made fewer financings than other investment companies, the average size of those financings was nearly four times larger (\$425,454 versus \$111,197). For less than 1 percent of the number of all financings and their dollar value, the ownership of the investment company making the financing was unknown. Bank-dominated investment companies typically financed relatively large companies and made financings that were somewhat more often used for acquiring existing businesses than was the case with other investment companies. Most bank-dominated investment companies that were active as of July 1990 had no SBA-guaranteed funds. (See sec. 4.)

To obtain information on the number and dollar amount of financings made by investment companies, the size of businesses receiving financing and the purpose of the financing, and the role of banks in providing financing through the SBIC and SSBIC programs, we analyzed SBA's automated records on investment companies' financings made to small businesses from January 1983 through December 1989. To obtain information on SBA's definition of "small business concern," we reviewed the applicable legislation and SBA regulations and interviewed officials in SBA's Investment Division and Office of General Counsel. (See sec. 5.)

Because our analysis relied on SBA's automated data, we discussed SBA's policy and procedures for maintaining the agency's data bases with representatives of SBA's Investment Division and assessed the data's accuracy and completeness. Although SBA's data bases on investment companies' financing activities have some limitations, they contain the most readily available information requested. (See app. I.) We did not attempt to evaluate the effectiveness of the SBIC and SSBIC programs. However, at the request of the Chairman of the Senate Small Business Committee, we are currently examining the causes of recent liquidations of investment companies.

We discussed the contents of this briefing report with officials of SBA's Investment Division. They generally concurred with our findings and conclusions, and we have incorporated their comments where appropriate. As requested, we did not obtain official agency comments.

Our work was conducted between August 1990 and February 1991 in accordance with generally accepted government auditing standards.

We are providing copies of this briefing report to the House and Senate Small Business Committees, the Administrator of SBA, the Director of the Office of Management and Budget, and other interested parties. We will make copies available to others upon request. Should you require any

---

additional information on the contents of this briefing report, please call me on (202) 275-5525. Major contributors to this briefing report are listed in appendix II.

Sincerely yours,

A handwritten signature in black ink that reads "John M. Ols, Jr." in a cursive script.

John M. Ols, Jr.  
Director, Housing and  
Community Development Issues



---

# Contents

---

Letter		1
Section 1 Number and Dollar Amount of Investment Companies' Financings		8
Section 2 Size of Businesses Receiving Financing		12
Section 3 Size Standards for Small Business Concerns		17
Section 4 Role of Bank- Dominated Investment Companies		18
Section 5 Objectives, Scope, and Methodology		24
Appendixes	Appendix I: Reliability Assessment	28
	Appendix II: Major Contributors to This Briefing Report	31
Table	Table I.1: Accuracy Test Results	29
Figures	Figure 1.1: Number of SBIC and SSBIC Financings	8
	Figure 1.2: Total Dollar Amount of SBIC and SSBIC Financings	9



---

Figure 1.3: Average Size of Individual SBIC and SSBIC Financings	10
Figure 1.4: Distribution of Financings, by Dollar Amount	11
Figure 2.1: Distribution of Financings, by Asset Size of the Recipient Business	13
Figure 2.2: Distribution of Financings, by Gross Revenue of the Recipient Business	14
Figure 2.3: Distribution of Financings, by Number of Employees of the Recipient Business	15
Figure 2.4: Purpose of Financings Made to Businesses With Assets of \$10 Million or More and Less Than \$10 Million	16
Figure 4.1: Total Dollar Amount of Financings Made by Bank-Dominated and Other Investment Companies	19
Figure 4.2: Distribution of Financings Made by Bank- Dominated and Other Investment Companies, by Asset Size of the Recipient Business	20
Figure 4.3: Distribution of Financings Made by Bank- Dominated and Other Investment Companies, by Gross Revenue of the Recipient Business	21
Figure 4.4: Distribution of Financings Made by Bank- Dominated and Other Investment Companies, by Number of Employees of the Recipient Business	22
Figure 4.5: Purpose of Financings Made by Bank- Dominated and Other Investment Companies	23

---

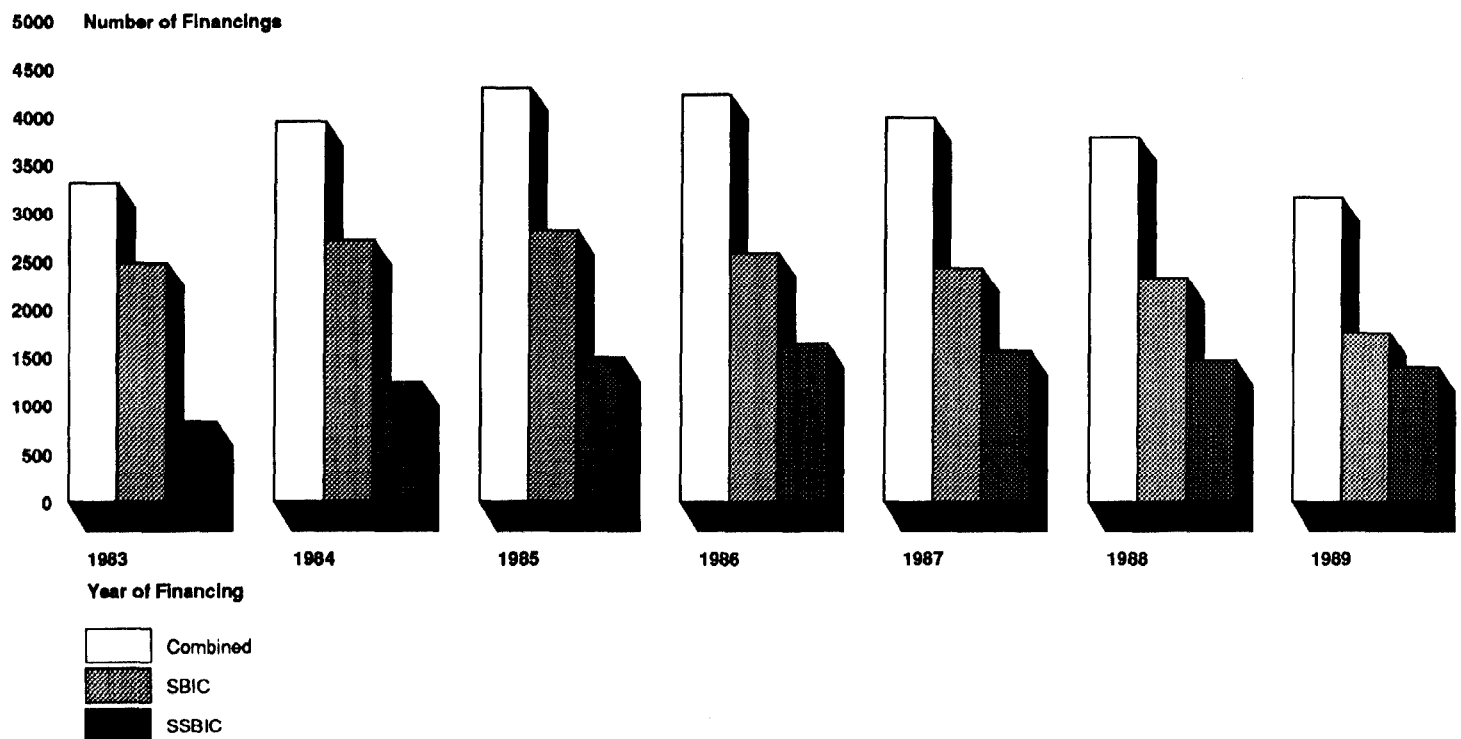
**Abbreviations**

GAO	General Accounting Office
SBA	Small Business Administration
SBIC	Small Business Investment Company
SSBIC	specialized Small Business Investment Company

# Number and Dollar Amount of Investment Companies' Financings

From 1983 to 1989, SBICs and SSBICs nationwide made 26,747 financings to small businesses totaling \$4.3 billion. While the number of financings has generally declined over the years, the total dollar amount of financings has generally increased. Specifically, the number of financings made by investment companies declined from a peak of 4,308 in 1985 to 3,162 in 1989. (See fig. 1.1.) It should be noted that the SBA data bases from which these numbers are drawn do not include records for between 5.2 and 11.5 percent of all financings. (See app. I for our analysis of the completeness of SBA's data bases.)

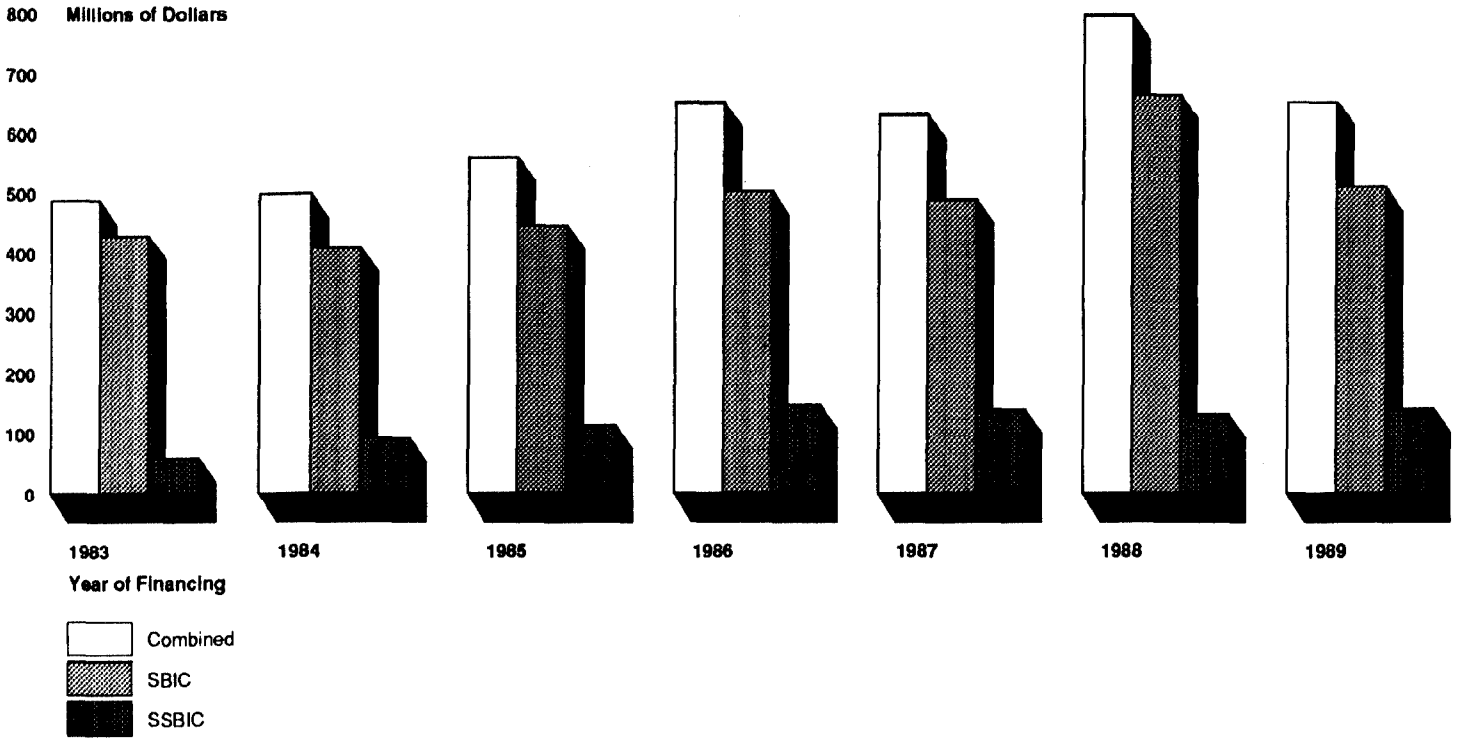
Figure 1.1: Number of SBIC and SSBIC Financings



The total dollar amount of investment companies' financings increased from \$488 million in 1983 to \$649 million in 1986, declined slightly in 1987, rose to \$796 million in 1988, and declined to \$653 million in 1989. For both SBICs and SSBICs, the total dollar amount of financings showed a similar pattern. (See fig. 1.2.)

Section 1  
Number and Dollar Amount of Investment  
Companies' Financings

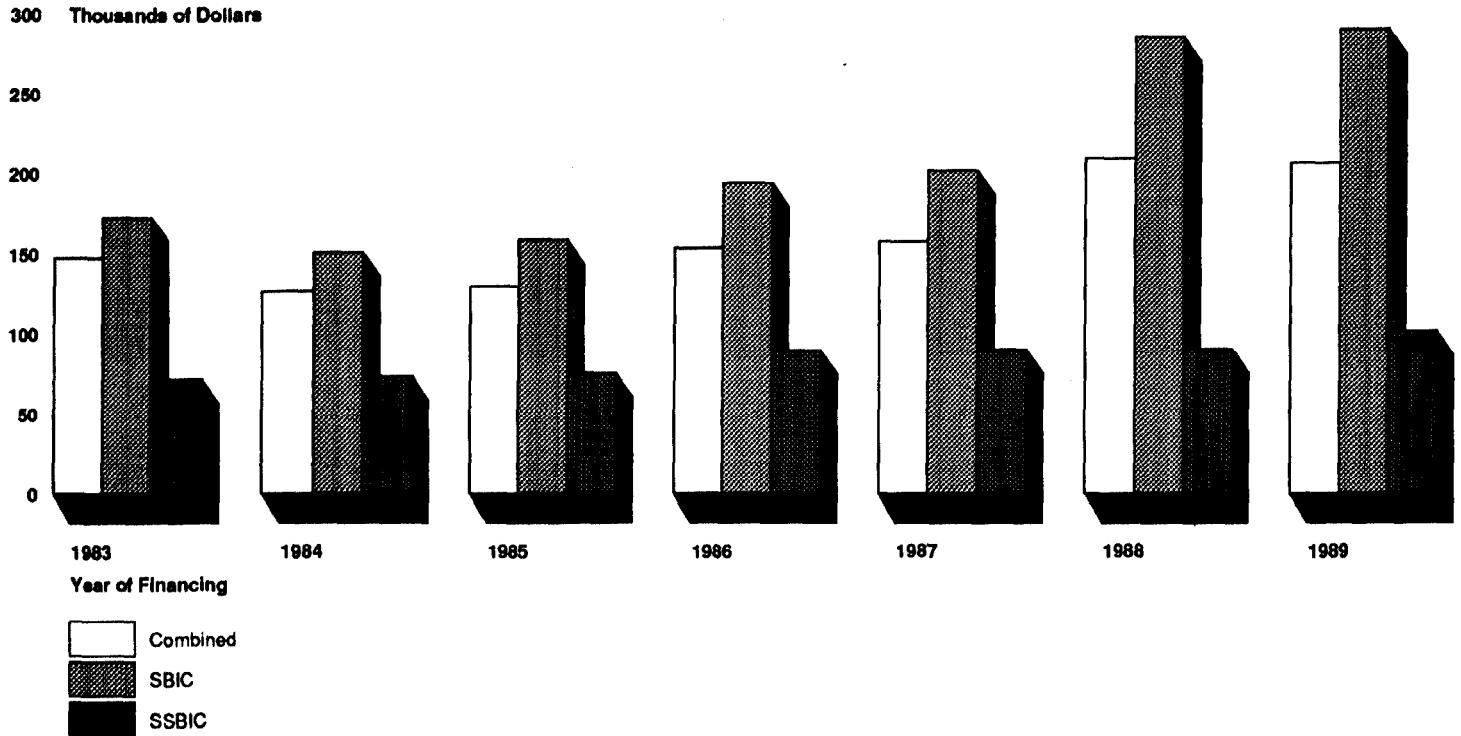
Figure 1.2: Total Dollar Amount of SBIC and SSBIC Financings



The average size of individual financings generally increased during these years. However, the increase was much greater for SBICs than for SSBICs: 68 percent compared with 42 percent. (See fig. 1.3.)

Section 1  
 Number and Dollar Amount of Investment  
 Companies' Financings

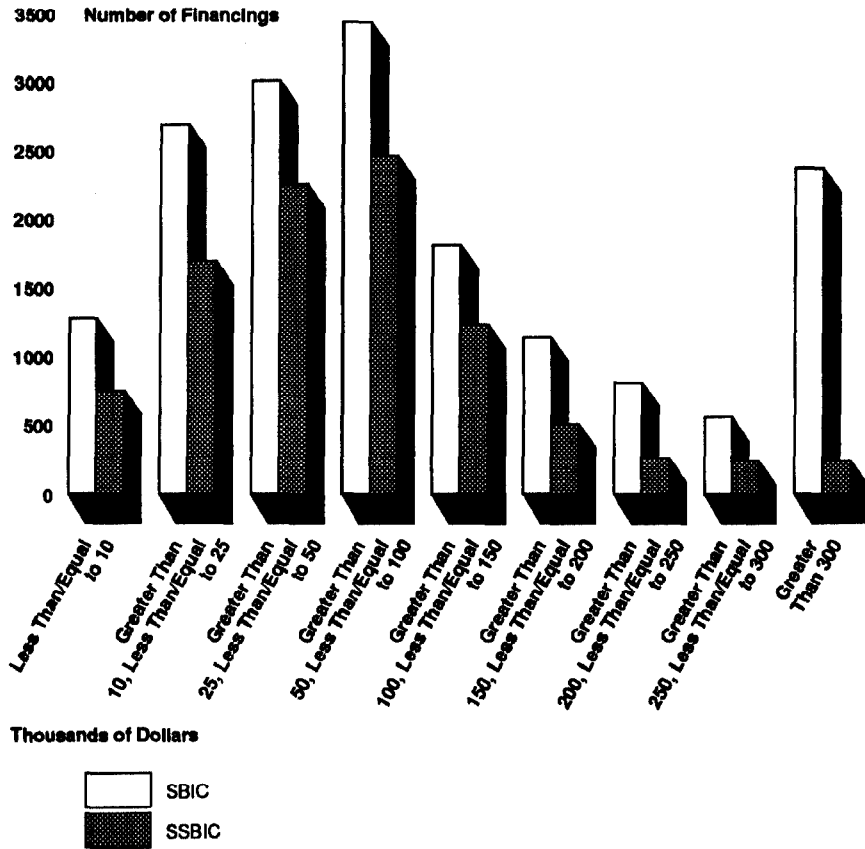
Figure 1.3: Average Size of Individual SBIC and SSBIC Financings



The median size of individual financings for this period was \$66,000. Typically, SBIC financings were larger than SSBIC financings. That is, the median sizes of SBIC and SSBIC financings were \$75,000 and \$55,000, respectively. Most financings for this period were between \$10,000 and \$100,000. SBICs accounted for a much greater proportion of the largest financings than did SSBICs. Of the 2,610 financings greater than \$300,000, 2,371, or 91 percent, were made by SBICs. (See fig. 1.4.)

Section 1  
 Number and Dollar Amount of Investment  
 Companies' Financings

Figure 1.4: Distribution of Financings, by Dollar Amount



Note: Data for 1983 through 1989.

---

# Size of Businesses Receiving Financing

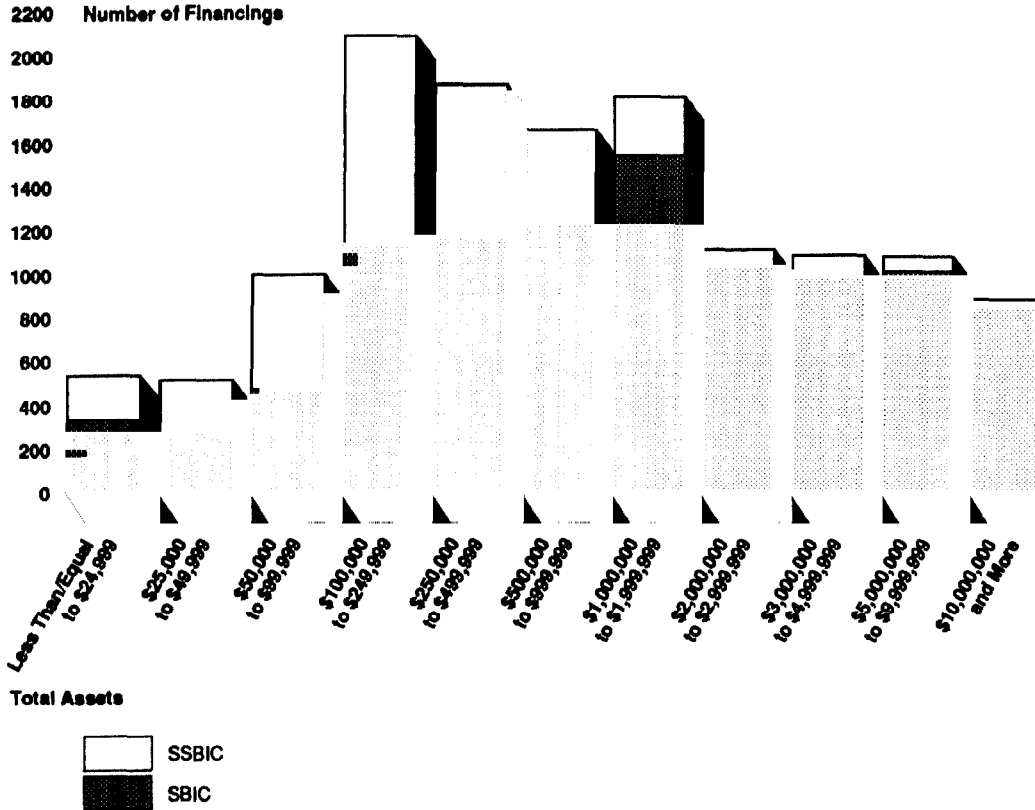
---

We examined SBA financing data for businesses whose sizes were recorded in the SBA data bases. It should be noted that size data—measured by total assets, gross revenue, and number of employees—were not available for a large percentage of the financings. Specifically, the SBA data bases had no data on the assets of the recipient business for 49 percent of all financings, no data on the gross revenue of the recipient business for 53 percent, and no data on the number of employees for 40 percent. SBA officials noted that this information may not be available if the recipient business has not completed an entire fiscal year or may be minimal if the business is new. Therefore, investment companies often do not provide these data for new businesses. Indeed, of the financings for which size data were missing, 60 percent occurred within 1 year of the date when the business was reportedly established. In addition, if a company receives more than one financing, SBA requires that size information be provided only once. Therefore, the data may have been missing in some records because they were provided earlier. However, this was clearly the case for only about 6 percent of financings, and we therefore did not substitute size data from earlier financings.

According to SBA data, between 1983 and 1989 over half of all financings for which size data were available were made to businesses that had less than \$1 million in total assets, less than \$1 million in gross revenue, and fewer than 20 employees. However, many financings were made to relatively larger companies, as measured by total assets, gross revenue, and number of employees. For example, 887 financings, or 6.5 percent of financings for which asset data were recorded, were made to businesses with assets of \$10 million or more. Similarly, 921 financings, or 7.4 percent of financings for which gross revenue data were recorded, were made to businesses with gross revenues of \$10 million or more. Also, 1,613 financings, or 10 percent of financings for which employee data were recorded, were made to businesses with 100 or more employees. Financings made to larger businesses were almost exclusively made by SBICS. (See figs. 2.1, 2.2, and 2.3.)

Section 2  
Size of Businesses Receiving Financing

Figure 2.1: Distribution of Financings, by Asset Size of the Recipient Business

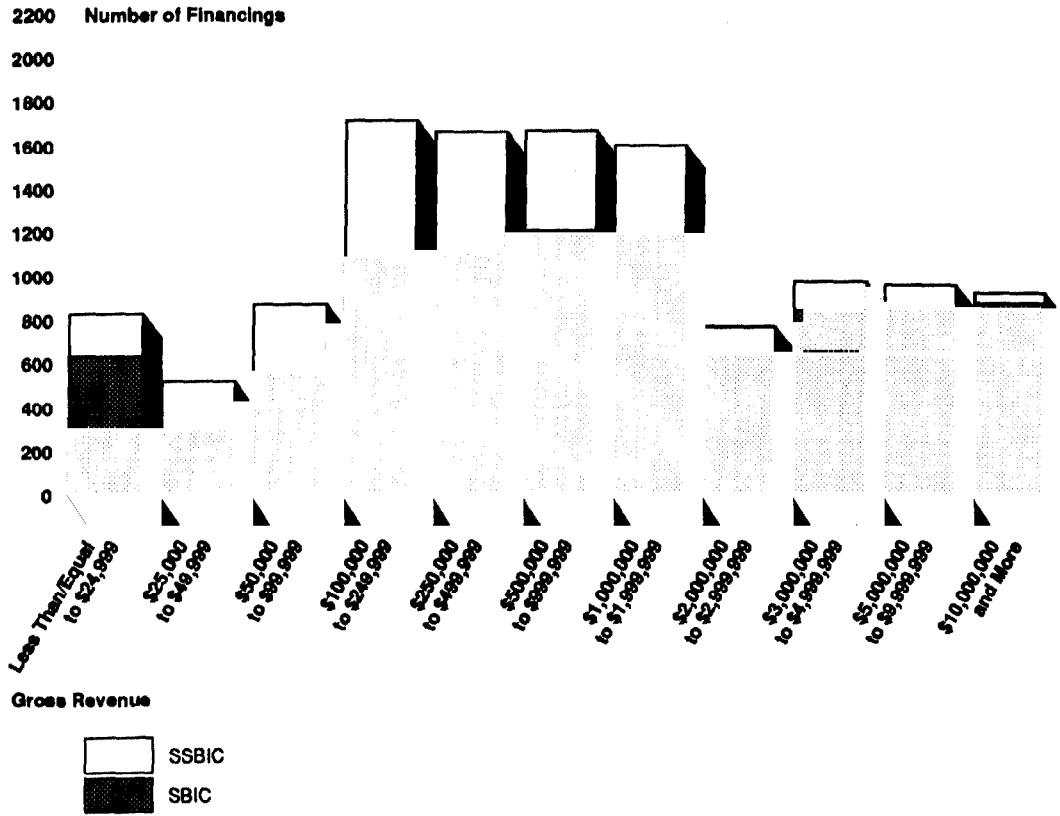


Notes: Data for 1983 through 1989.

For 7,045 SBIC financings, or 41.2 percent of all SBIC financings, and for 6,058 SSBIC financings, or 62.9 percent of all SSBIC financings, the assets of the business receiving the financing were unknown.

**Section 2**  
**Size of Businesses Receiving Financing**

**Figure 2.2: Distribution of Financings, by Gross Revenue of the Recipient Business**

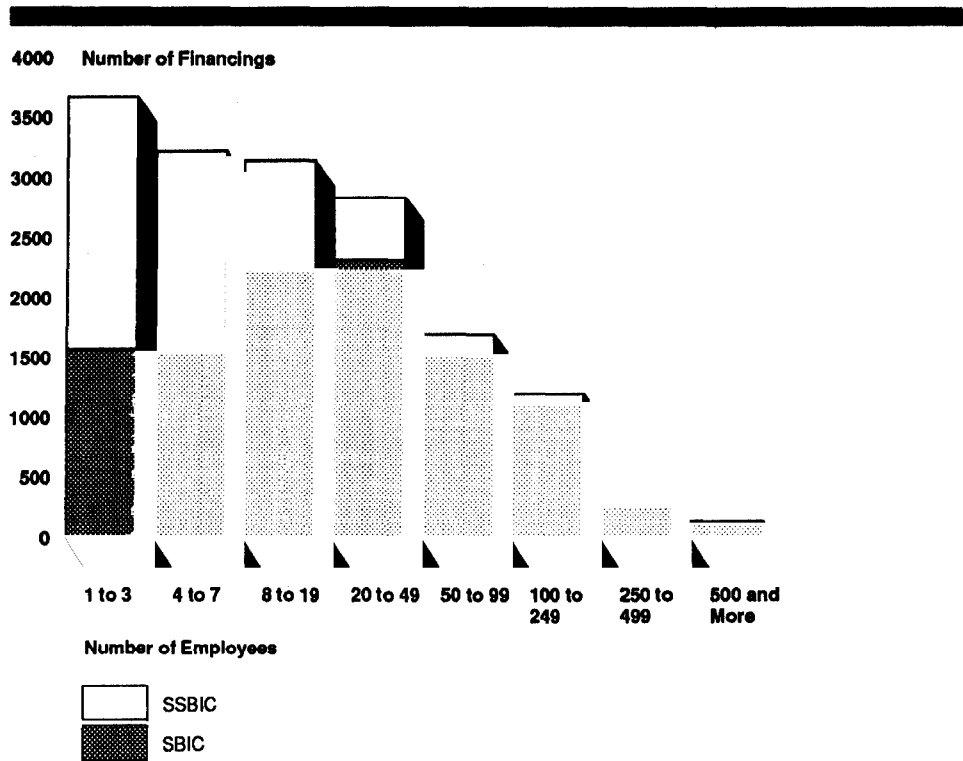


Notes: Data for 1983 through 1989.

For 7,825 SBIC financings, or 45.7 percent of all SBIC financings, and for 6,460 SSBIC financings, or 67.0 percent of all SSBIC financings, the gross revenue of the business receiving the financing was unknown.



**Figure 2.3: Distribution of Financings, by Number of Employees of the Recipient Business**



Notes: Data for 1983 through 1989.

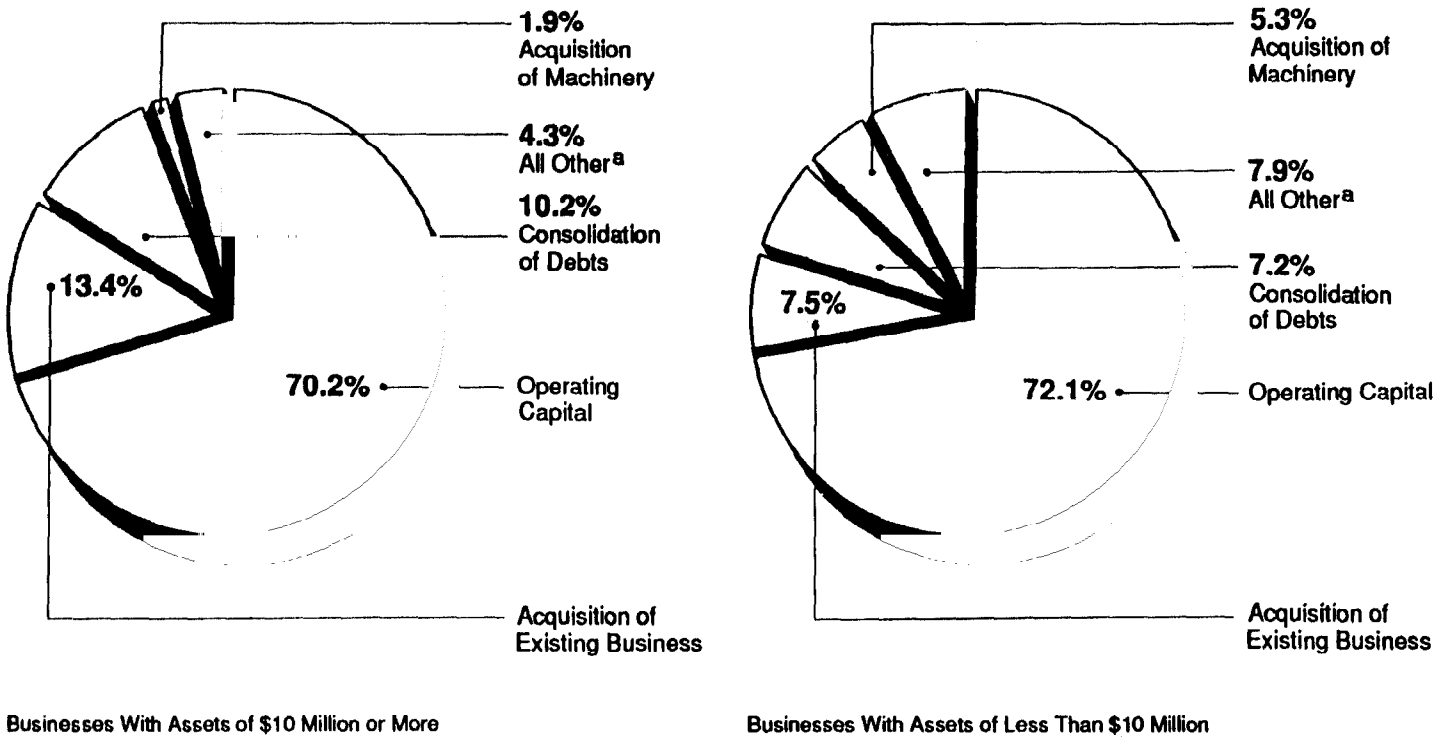
For 6,423 SBIC financings, or 37.5 percent of all SBIC financings, and for 4,172 SSBIC financings, or 43.3 percent of all SSBIC financings, the number of employees of the business receiving the financing was unknown.

Most financings for companies with both large and small total assets were used for operating capital. As noted above, the SBA data bases had no data on the assets of the recipient business for 49 percent of all financings. For companies with assets of \$10 million or more, 623 financings, or 70.2 percent, were used for operating capital; for companies with assets of less than \$10 million, 9,193 financings, or 72.1 percent, were used for operating capital. However, financings made to businesses with assets in excess of \$10 million were almost twice as likely to be used to acquire an existing business. Specifically, while 953 financings to businesses with less than \$10 million in assets, or 7.5 percent of such financings for which SBA recorded asset data, were used to acquire an existing business; 119 financings made to businesses with assets of \$10 million or more, or 13.4 percent of such financings for which SBA recorded asset data, were used for that purpose. (See fig. 2.4.) Where asset size was unknown, 16.3 percent of financings were used to

**Section 2**  
**Size of Businesses Receiving Financing**

acquire an existing business. Furthermore, of the largest 100 financings, 59 funded the acquisition of an existing business.

**Figure 2.4: Purpose of Financings Made to Businesses With Assets of \$10 Million or More and Less Than \$10 Million**



<sup>a</sup>Includes plant modernization, construction of a new building or plant, acquisition of land, marketing, and research and development.

Note: Data for 1983 through 1989.

# Size Standards for Small Business Concerns

As mentioned earlier, the SBIC and SSBIC programs were created to help small businesses obtain equity capital, management assistance, and long-term financing. In general, SBA regulations define small business concerns by net worth and income. Specifically, title 13 of the Code of Federal Regulations, section 121.802(a)(2), requires that an applicant business meet one of two size standards. The first requires that the business have \$6 million or less in net worth and \$2 million or less in annual average net income after federal income taxes for the preceding 2 completed fiscal years. The second size standard by which a business may qualify for SBIC financing is that used by other SBA programs. This size standard varies by industry and, with few exceptions, involves measures of annual receipts and number of employees. SBA is reviewing the size standards used in the SBIC program with the expectation of increasing the acceptable size limits for net worth and net income, and in September 1990 SBA proposed an asset size criterion.

Because the size standards used to determine whether a business is a small business concern do not currently include measures of asset size, companies with large assets may qualify as a small business. For example, a company may meet the \$6-million net worth standard even if it has large assets, so long as its assets exceed its liabilities by no more than \$6 million and its annual average net income after federal income taxes was \$2 million or less.

In recognition of SBA's concerns that businesses were receiving SBIC financing for leveraged buy-outs of companies with large assets, SBA proposed regulations in September 1990 that would limit to \$20 million the gross assets of a business whose change of ownership can be financed by an SBIC. This proposed limit is based on a \$9-million asset limit that was in effect between August 1975 and September 1979 for all types of SBIC financings, adjusted for inflation. As proposed, the new limit would apply only to SBIC financings whose purpose is the acquisition of an existing business. Of the 26,747 financings made between 1983 and 1989, 23,538, or 88 percent, were for purposes other than acquiring an existing business. SBA is currently reviewing the net worth and net income size standards applicable to the SBIC program with a view to increasing them.

# Role of Bank-Dominated Investment Companies

---

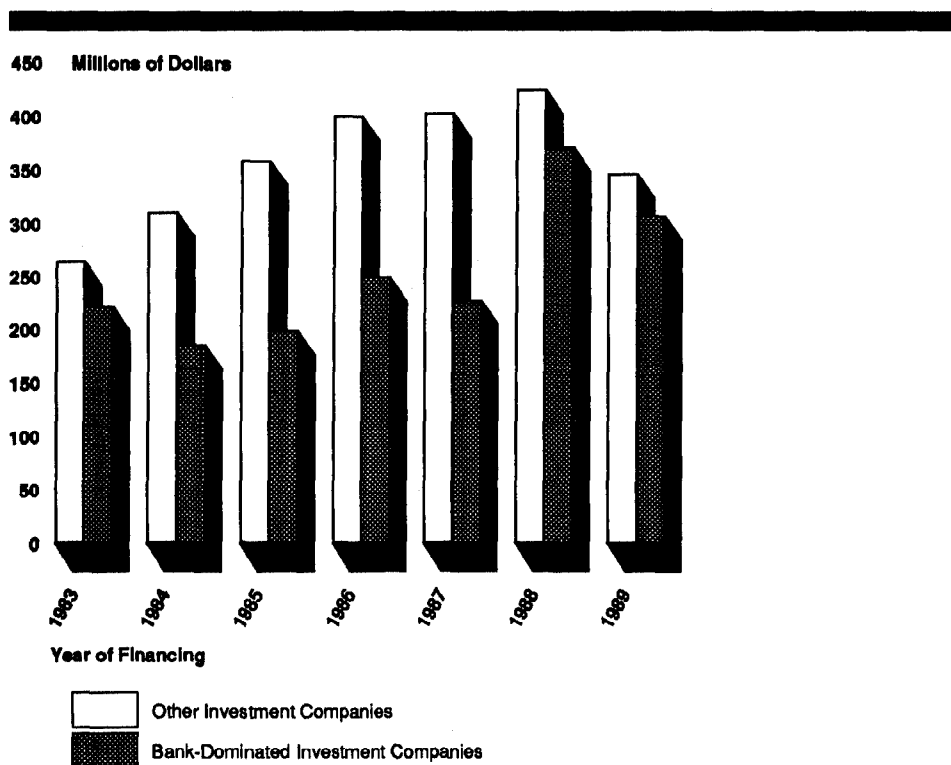
As of July 1990, banks had at least a 50-percent ownership in 86 SBICs and 6 SSBICs, or 34 percent of all SBICs and 5 percent of all SSBICs. These SBICs and SSBICs, called "bank dominated," play a significant role in SBA's investment company program. Bank-dominated investment companies, many without the use of SBA-guaranteed funds, provided nearly half of all SBIC and SSBIC financing dollars from 1983 to 1989. Financings made by bank-dominated investment companies were typically much larger, were more often made to larger businesses, and were more often used for acquiring existing businesses than were financings made by other investment companies.

Bank-dominated investment companies have relied more on their own capital, without the benefit of SBA-guaranteed funds, to finance small business concerns than other investment companies. Specifically, of the 92 bank-dominated investment companies active as of July 1990, 64, or about 70 percent, had no SBA-guaranteed funds. Conversely, of the 297 other investment companies active as of July 1990, 62, or about 21 percent, had no SBA-guaranteed funds. Furthermore, while bank-dominated investment companies had \$7.10 in private capital for every dollar of SBA investment, other investment companies had only \$0.80.

Nationwide, financings by bank-dominated investment companies totaled \$1.8 billion, or 41 percent of the total funds provided from 1983 to 1989. Bank-dominated investment companies made fewer financings than other investment companies, but the size of those financings was much larger. Specifically, bank-dominated investment companies made 4,133 financings between 1983 and 1989, or about 16 percent of all financings. The average size of these financings was \$425,454—four times the size of financings made by other investment companies. (For less than 1 percent of the number and dollar amount of all financings, the ownership of the investment company was unknown. We therefore excluded these financings from our analysis of investment company ownership.) Furthermore, of the 100 largest financings, 85 were made by bank-dominated investment companies. In recent years, the share of funds provided by bank-dominated investment companies has increased and in 1989 represented about 47 percent of the total funds provided by all investment companies. (See fig. 4.1.)

**Section 4  
Role of Bank-Dominated  
Investment Companies**

**Figure 4.1: Total Dollar Amount of  
Financings Made by Bank-Dominated  
and Other Investment Companies**

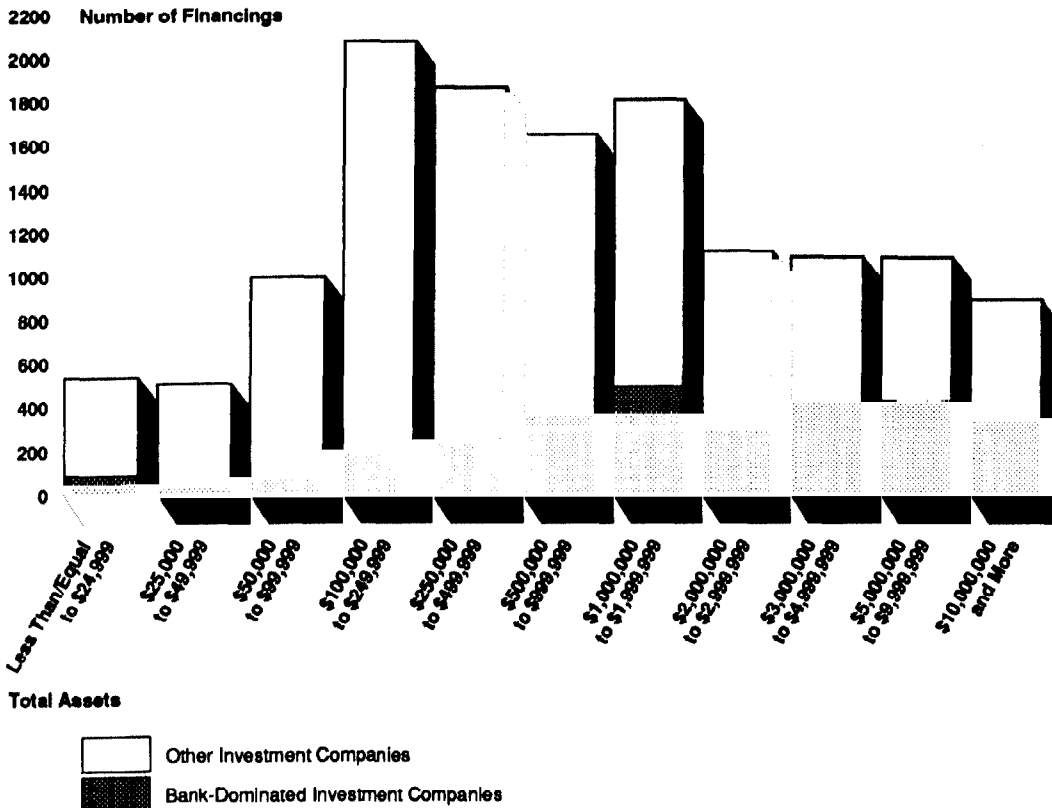


Note: For 97 financings totaling \$10 million, or 0.4 percent of the number of all financings and 0.2 percent of their dollar value, the investment company making the financing was not included in either SBA's data bases on active investment companies or previous directories. Since we could not identify the ownership of the investment company for these financings, we did not include them in our analysis of investment company ownership.

Bank-dominated investment companies typically financed larger businesses—as measured by total assets, gross revenue, and number of employees—than did other investment companies. For example, while 11.6 percent of financings made by bank-dominated investment companies went to businesses with assets of \$10 million or more, 5.1 percent of financings made by other investment companies went to businesses of that size. (See fig. 4.2.) As noted earlier, for about half of all financings, data on the assets, gross revenue, and/or number of employees of the business being financed were not recorded in SBA's data bases. We therefore excluded these financings from our analysis of business size.

**Section 4  
Role of Bank-Dominated  
Investment Companies**

**Figure 4.2: Distribution of Financings Made by Bank-Dominated and Other Investment Companies, by Asset Size of the Recipient Business**



Notes: Data for 1983 through 1989.

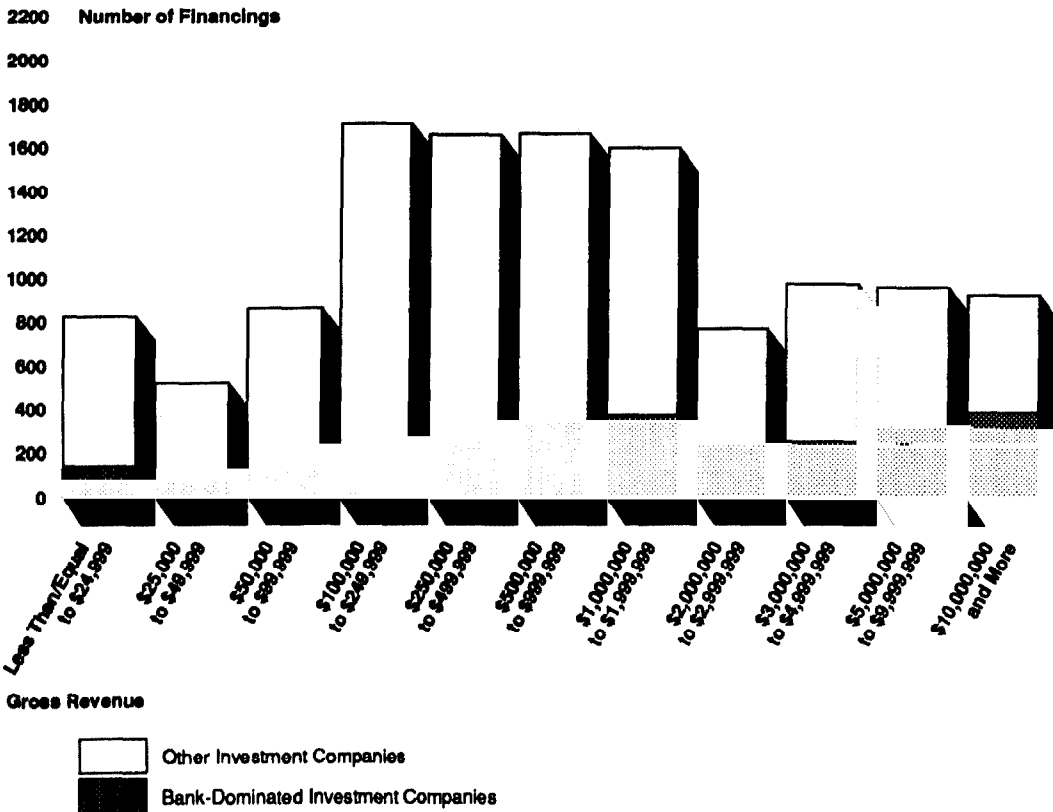
For 1,175 financings made by bank-dominated companies, or 28.4 percent of those financings, and 11,897 financings made by other investment companies, or 52.8 percent of those financings, the assets of the recipient business were unknown.

For 97 financings totaling \$10 million, or 0.4 percent of the number of all financings and 0.2 percent of their dollar value, the investment company making the financing was not included in either SBA's data bases on active investment companies or previous directories. Since we could not identify the ownership of the investment company for these financings, we did not include them in our analysis of investment company ownership.

Financings made by bank-dominated investment companies typically went to businesses with larger gross revenues than did financings made by other investment companies. Specifically, while 14.1 percent of financings made by bank-dominated investment companies went to businesses with gross revenues of \$10 million or more, 5.6 percent of financings made by other investment companies went to such businesses. (See fig. 4.3.)

**Section 4  
Role of Bank-Dominated  
Investment Companies**

**Figure 4.3: Distribution of Financings Made by Bank-Dominated and Other Investment Companies, by Gross Revenue of the Recipient Business**



Notes: Data for 1983 through 1989.

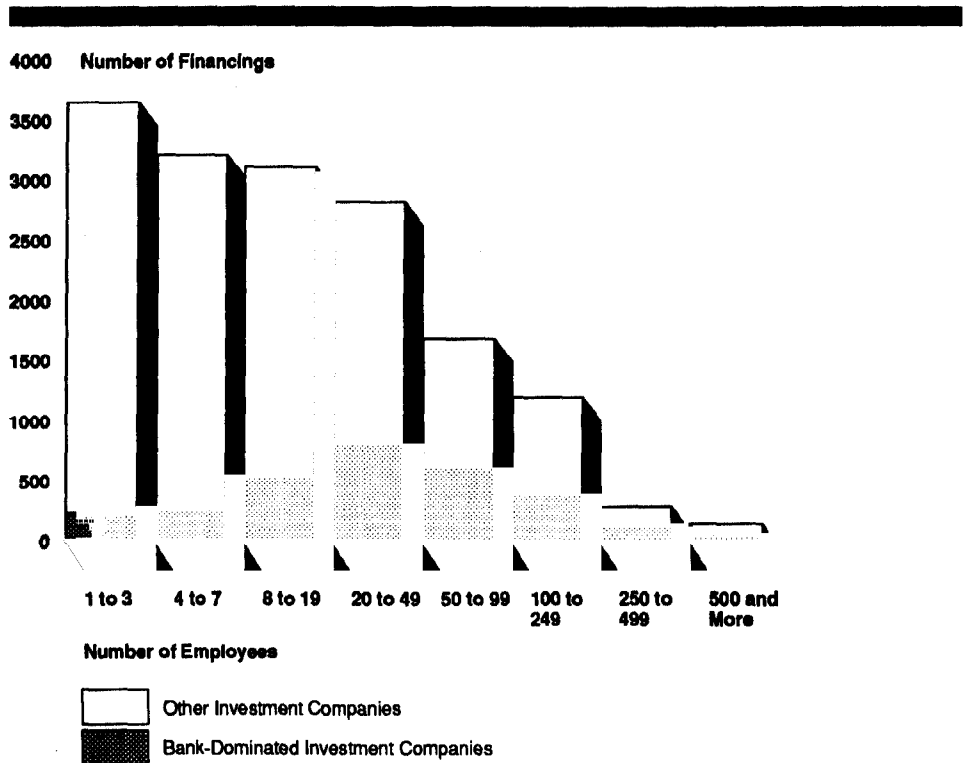
For 1,437 financings made by bank-dominated companies, or 34.8 percent of those financings, and 12,817 financings made by other investment companies, or 56.9 percent of those financings, the gross revenue of the recipient business was unknown.

For 97 financings totaling \$10 million, or 0.4 percent of the number of all financings and 0.2 percent of their dollar value, the investment company making the financing was not included in either SBA's data bases on active investment companies or previous directories. Since we could not identify the ownership of the investment company for these financings, we did not include them in our analysis of investment company ownership.

Finally, while bank-dominated investment companies made 558 financings, or 18.4 percent of all their financings, to businesses with 100 or more employees, other investment companies made 1,053 financings, or 8.1 percent of all their financings, to such businesses. (See fig. 4.4.)

**Section 4  
Role of Bank-Dominated  
Investment Companies**

**Figure 4.4: Distribution of Financings Made by Bank-Dominated and Other Investment Companies, by Number of Employees of the Recipient Business**



Notes: Data for 1983 through 1989.

For 1,105 financings made by bank-dominated companies, or 26.7 percent of those financings, and 9,461 financings made by other investment companies, or 42.0 percent of those financings, the number of employees of the recipient business was unknown.

For 97 financings totaling \$10 million, or 0.4 percent of the number of all financings and 0.2 percent of their dollar value, the investment company making the financing was not included in either SBA's data bases on active investment companies or previous directories. Since we could not identify the ownership of the investment company for these financings, we did not include them in our analysis of investment company ownership.

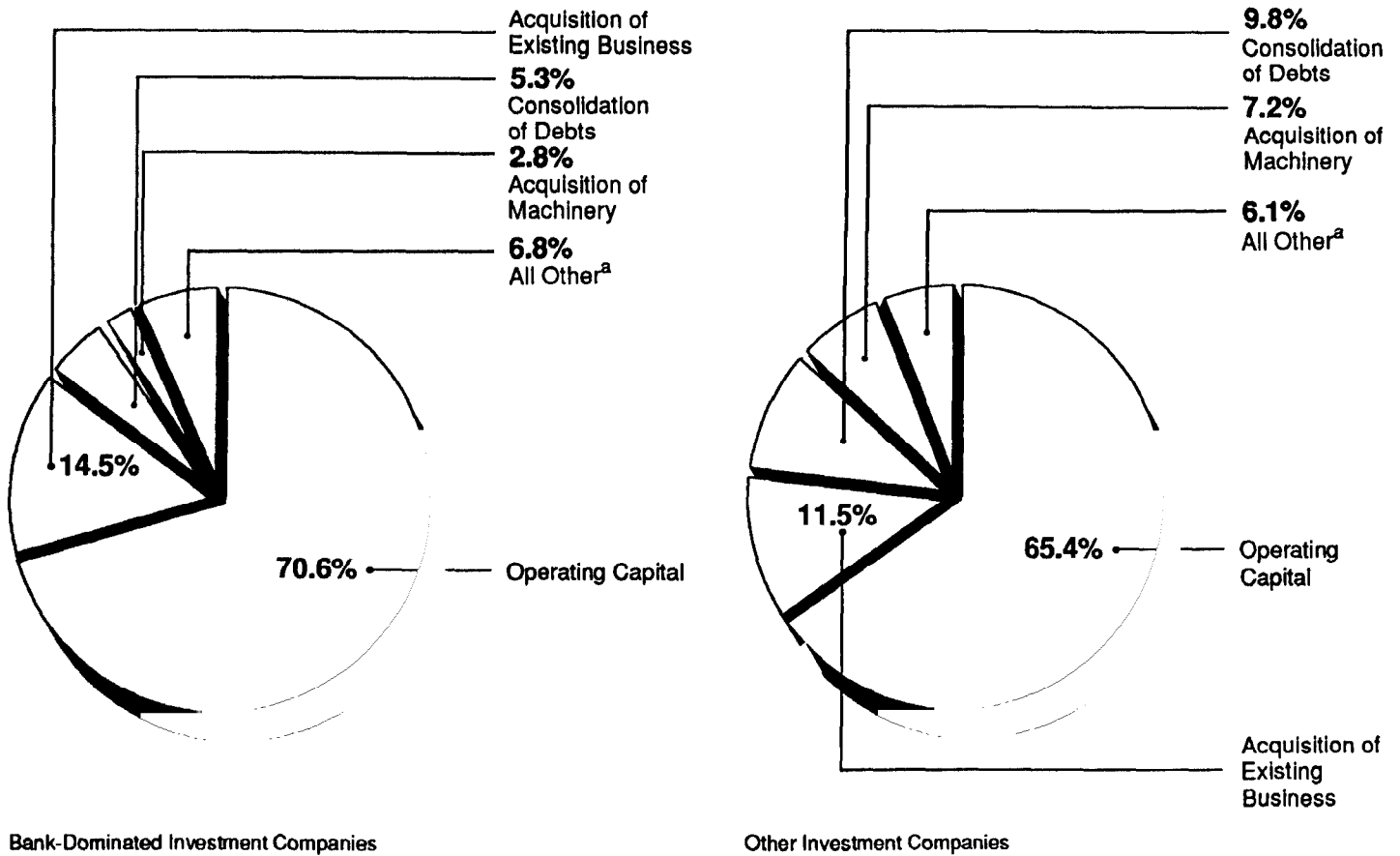
Bank-dominated investment companies made a larger share of their financings for the purpose of acquiring an existing business than did other investment companies. Specifically, of the 4,133 financings made by bank-dominated investment companies, 601, or 14.5 percent, were made for the purpose of acquiring an existing business. By contrast, of the 22,517 financings made by other investment companies, 2,599, or 11.5 percent, were made for that purpose. Financings by bank-dominated investment companies were also more often made for research and development (3.0 percent versus 1.0 percent). Financings by bank-dominated investment companies were less often made for modernizing plants (0.8 percent versus 2.1 percent), consolidating debt (5.3 percent



**Section 4**  
**Role of Bank-Dominated**  
**Investment Companies**

versus 9.8 percent), and acquiring machinery (2.8 percent versus 7.2 percent). (See fig. 4.5.)

**Figure 4.5: Purpose of Financings Made by Bank-Dominated and Other Investment Companies**



<sup>a</sup>Includes plant modernization, construction of a new building or plant, acquisition of land, marketing, and research and development.

Notes: Data for 1983 through 1989.

For 97 financings totaling \$10 million, or 0.4 percent of the number of all financings and 0.2 percent of their dollar value, the investment company making the financing was not included in either SBA's data bases on active investment companies or previous directories. Since we could not identify the ownership of the investment company for these financings, we did not include them in our analysis of investment company ownership.

# Objectives, Scope, and Methodology

Citing concerns that large businesses were receiving financing from SBICs and SSBICs, Representative Marty Russo requested that we analyze the amount of SBIC financing being made to corporations and the relative sizes of those recipient corporations. In subsequent discussions with his staff, we agreed to analyze (1) the number and dollar amount of these financings, (2) the size of businesses receiving financing and the purpose of the financing, (3) SBA's definition of small business and the ability of businesses with large gross assets to qualify as small business concerns, and (4) the role of banks in providing financing through the SBIC and SSBIC programs. In addition, because our analysis relied on SBA's automated data, we discussed SBA's policy and procedures for maintaining the agency's data bases with representatives of SBA's Investment Division and assessed the accuracy and completeness of SBA's financing data bases. (See app. I.)

SBA's Investment Division maintains data bases on SBIC and SSBIC financing activities. These data bases include selected information from periodic reports that the investment companies are required to file with SBA (Portfolio Financing Report, SBA Form 1031) each time they make a new financing. We obtained automated records on small business financings that had been updated as of August 30, 1990. We used records of financings that were dated between January 1, 1983, and December 31, 1989. We selected December 1989 as the end date for the records examined because it was the latest calendar year for which data input should have been completed when we received the data in September 1990. The automated records we received from SBA did not include 32 financing records from 1989, including 5 duplicate records that SBA had subsequently entered into its data bases. SBA compiles data on financings according to the dates it receives the financing reports rather than the actual dates the financings were made. SBA regulations require that SBICs and SSBICs file a portfolio financing report with the SBA within 15 days after the date of the financing. SBA includes in the data bases those reports that the Investment Division receives within 6 months after the date of the financing. Before January 1989, the cutoff period for SBIC financings was 3 months. Because of this lag, some financings do not reflect the actual year in which they originated. For example, an SBIC financing originating in November 1987 but reported to SBA in January 1988 would be reported with SBA's 1988 calendar year data. To obtain a truer representation of the activity actually occurring within a given calendar year, we based our analysis on the actual date of the financing rather than on SBA's reported date. Accordingly, our annual statistics differ from SBA's.

The Investment Division maintains a data base file on all active investment companies, which serves as the basis for semi-annual directories of investment companies. This file includes information on the name, license number, and type of ownership of SBICs and SSBICs. Because some financings were made by investment companies that are no longer active, we used automated records on investment companies that were active as of August 1990, June 1989, and December 1987. We also used historical records on active investment companies for earlier years.

To determine the number and dollar amount of financings made by SBICs and SSBICs, we analyzed SBA's data bases on SBIC and SSBIC financings. Using statistical software we analyzed financings by the year in which they were made and by their number, dollar amount, and average size. All records in the data bases included data on the dollar amount of individual financings. Because SBIC and SSBIC financings sometimes significantly differ, those differences are presented in our analysis.

To analyze the size of businesses receiving financing, we used information from SBA's data bases on investment companies' financing activities. We compared the number of financings made by SBICs and SSBICs with the size of the small business concerns receiving the financing. We measured size using total assets, gross revenue, and number of employees—the only measures of company size that SBA enters into its financing data base. Furthermore, because SBA maintains company size data in ranges rather than as exact amounts, we were restricted to those ranges in analyzing the size of recipient companies. To analyze the extent to which companies with large assets use SBIC and SSBIC financings to acquire existing businesses, we also compared the purposes for which financings were used by businesses with assets of less than \$10 million and those with assets of \$10 million or more. Many financing records in the data bases had no entry for the three measures of company size. Officials from SBA's Investment Division explained that such data may not be available for new businesses. Indeed, of the financings for which size data were missing, 60 percent occurred within 1 year of the date when the business was reportedly established. In addition, if a company receives more than one financing, SBA requires that size information be provided only once. Therefore, the data may have been missing in some records because they were provided earlier. However, this was clearly the case for only about 6 percent of financings, and we therefore did not substitute size data from earlier financings.

To determine how businesses with large gross assets can qualify as a small business concern, we reviewed the size standards now in effect, as

well as previous and proposed regulatory standards. We also discussed the definition of small business concern with officials in SBA's Investment Division and Office of General Counsel.

To analyze the role of banks in providing financing through the SBIC and SSBIC programs, we used data from SBA's financing data bases and SBA's August 1990, June 1989, and December 1987 data bases on active SBICS and SSBICS, as well as directories of investment companies from December 1986, December 1985, December 1984, and June 1983. To determine whether a financing was made by a bank-dominated investment company, we corrected erroneous license numbers in the financing data bases on the basis of the licensee name and then merged the automated data bases using license number. When we were unable to match the licensee number from the financing data bases with a licensee number from the three data bases on active SBICS, we entered the ownership type from the directories of investment companies listed above. We sorted financings made by bank-dominated and other investment companies on the basis of the year in which the financing was made. We also compared the sizes of businesses receiving financing from bank-dominated and other investment companies in terms of total assets, gross revenue, and number of employees.

We conducted our work at SBA headquarters, in Washington, D.C., between August 1990 and February 1991 in accordance with generally accepted government auditing standards.

We discussed the report's contents with officials of SBA's Investment Division. These officials generally agreed that the report fairly represents the data on SBIC and SSBIC financings made to small business concerns, and we have incorporated their comments where appropriate. As agreed with Representative Russo's office, we did not obtain official comments from SBA.



---

# Reliability Assessment

---

Because the analysis contained in this report depends, to a large extent, on data found in SBA's data bases of SBIC and SSBIC financing activities, we assessed the reliability of these data. We tested whether the proper data from the required forms were accurately and completely captured in the data bases. The first test, on the accuracy of SBA's data bases, involved comparing a sample of records from the data bases with original documents in storage. The second test, on the completeness of SBA's data bases, involved drawing a sample of the original documents in storage and verifying their presence in, or absence from, the data bases. After performing these tests, we used various statistical programs to calculate point estimates of the percentages of errors and completeness.

Since we used a sample (called a probability sample) in each test to develop our estimates, each estimate has a measurable precision, or sampling error, which may be expressed as a plus/minus figure. A sampling error indicates how closely we can reproduce from a sample the results that we would obtain if we were to completely test the universe using the same methods. By adding the sampling error to and subtracting it from the estimate, we can determine the lower and upper bounds for each estimate. This range is called a confidence interval. Sampling errors and confidence intervals are stated at a certain confidence level—in this case, 95 percent. A confidence interval at the 95-percent confidence level means that in 95 out of 100 instances the sampling procedures we used would produce a confidence interval containing the universe value we are estimating.

---

## Accuracy Test

From the 26,834<sup>1</sup> financing records for calendar years 1983 through 1989 in SBA's computer files, we drew a random sample of 300 records. We compared 23 fields from each record in the data base with the entries on each original document filed at SBA headquarters. Of the 6,900 entries we checked, 80, or 1.16 percent, were incorrectly entered into the data base. (See table I.1.)

---

<sup>1</sup>This figure includes 87 duplicate financing records, which we excluded from our analysis.

**Appendix I  
Reliability Assessment**

**Table I.1: Accuracy Test Results**

SBA data base field name	Number of errors	Estimated percentage of records in error	Confidence level (95%)	
			Lower bound of error (percent)	Upper bound of error (percent)
Control number	4	1.3	0.37	3.37
Business name	3	1.0	0.21	2.88
State	0	<sup>a</sup>	0.00	0.99
Zip code	7	2.3	0.95	4.74
Date established <sup>b</sup>	22 <sup>c</sup>	7.3	4.67	10.87
Form	0	<sup>a</sup>	0.00	0.99
SIC code	2	0.7	0.08	2.38
Employees <sup>b</sup>	6	2.0	0.74	4.29
Gross revenue <sup>b</sup>	4	1.3	0.37	3.37
Total assets <sup>b</sup>	5	1.7	0.54	3.84
Date financed <sup>b</sup>	3	1.0	0.21	2.88
Total <sup>b</sup>	0	<sup>a</sup>	0.00	0.99
Purpose <sup>b</sup>	8	2.7	1.16	5.18
Debt	0	<sup>a</sup>	0.00	0.99
Debt/equity	0	<sup>a</sup>	0.00	0.99
Equity	0	<sup>a</sup>	0.00	0.99
Interest rate	5	1.7	0.54	3.84
First financing	4	1.3	0.37	3.37
Management service	3	1.0	0.21	2.88
Contract	1	0.3	0.01	1.84
Repurchase equity	1	0.3	0.01	1.84
SBIC name <sup>b</sup>	0	<sup>a</sup>	0.00	0.99
License number <sup>b</sup>	2	0.7	0.08	2.38
Overall	80	1.16	0.92	1.44

<sup>a</sup>Since we observed no errors, we provide only the lower and upper bounds for the estimate using a hypergeometric distribution.

<sup>b</sup>Used in this report.

<sup>c</sup>Year is accurate for all but 3 of the 300 records examined. The year and month were accurate for all but 8 of the 300 records examined.

## Completeness Test

To test the completeness of the data bases, we relied upon a test we performed in 1988. At that time, we checked to see whether a sample of 326 hard-copy financing records from SBA's storage files were contained in SBA's automated data bases. We observed that 38 records were absent from the data bases. According to SBA officials, 13 of these records did not need to be filed and should therefore have been excluded from the count of omitted records, leaving 25 omitted records out of a sample of

313. These 25 records were omitted either because the investment company filed late or because of an oversight. At the 95-percent confidence interval, we estimate that 5.2 to 11.5 percent of all hard-copy records were not included in the automated data bases. Most of the omissions (22 of the 25) occurred because investment companies had submitted their financing reports to SBA late. Under SBA policy, financing records submitted by SBICs and SSBICs more than 6 months after the date of a financing are filed in hard-copy form but not entered into the data base. We found that the data in the sample of missing records in our 1988 test were not substantially different from those in the automated file. We therefore believe that the exclusion of information from missing records did not impair our analysis of overall trends in SBIC and SSBIC financing activities. However, the omission of financing records would cause the totals we have reported on investment companies' financing activities to be understated by the dollar amount of the true percentage of missing records. We did not project the dollar value, however, because of the wide variance in our estimate of the missing records.



---

# Major Contributors to This Briefing Report

---

Resources,  
Community, and  
Economic  
Development Division,  
Washington, D.C.

James R. Yeager, Assistant Director  
Mathew J. Scire, Evaluator-in-Charge  
Thomas F. Noone, Senior Systems Analyst



---

### **Ordering Information**

**The first five copies of each GAO report are free. Additional copies are \$2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.**

**U.S. General Accounting Office  
P.O. Box 6015  
Gaithersburg, MD 20877**

**Orders may also be placed by calling (202) 275-6241.**

---

**United States  
General Accounting Office  
Washington, D.C. 20548**

**Official Business  
Penalty for Private Use \$300**

**First-Class Mail  
Postage & Fees Paid  
GAO  
Permit No. G100**

---