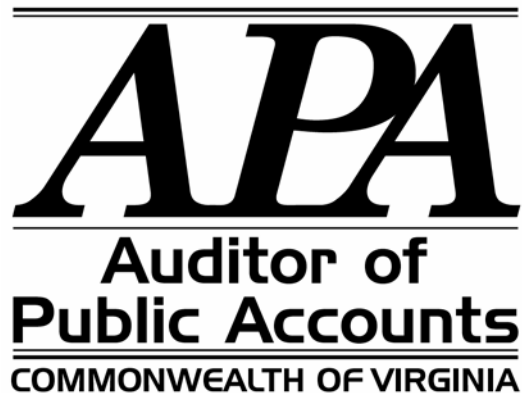


**VIRGINIA SMALL BUSINESS
FINANCE AUTHORITY**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2006**



AUDIT SUMMARY

Our audit of the Virginia Small Business Finance Authority for the year ended June 30, 2006, found:

- the Authority transferred the largest and most significant state loan program, the Virginia Economic Development Loan Program, to a newly created community development financial institution as a requirement of the 2005 Virginia Acts of the Assembly;
- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- no matters involving internal control and its operations necessary to bring to management's attention; and
- no instances of noncompliance with applicable laws and regulations or other matters that are required to be reported.

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AUTHORITY HIGHLIGHTS

The Virginia Small Business Finance Authority provides Virginia's businesses access to capital through public financing in an effort to maximize employment opportunities throughout the Commonwealth. The Authority provides this assistance through the various assistance programs.

The Department of Business Assistance houses the Authority and pays certain administrative expenses. The Director of the Department of Business Assistance appoints the Authority's Executive Director, and the board of directors, appointed by the Governor, oversee the Authority's operations. The operations of the Authority consist of reviewing program applications, conducting credit analysis, monitoring the progress of projects that have received funding, and servicing loan receivables. In addition, the Authority monitors the state ceiling for the Virginia Private Activity Bond Allocation. This allocation consists of the Industrial Development Bond Allocation, the Housing Bond Allocation, and the Governor's State Allocation.

SIGNIFICANT EVENT AND OTHER PROGRAMS

During fiscal year 2006, the Authority transferred nearly \$7.9 million in assets from the Virginia Economic Development Revolving Fund, consisting of cash and receivables, to the newly created Virginia Community Capital Bank as required by the 2005 Virginia Acts of the Assembly. This fund was the state-funded component of the Economic Development Loan Program. The following chart highlights the various programs administered by the Authority.

<u><i>Child Care Financing Program</i></u> provides assistance to family home providers and childcare centers through installment loans. The borrower can use the loans to either enhance the quality of care or meet or maintain state or local childcare requirements, including health, safety, and fire codes.	<u><i>Loan Guaranty Program</i></u> provides participating local banks deficiency loan guarantees for loans made to Virginia businesses that do not have access to capital. Borrowers contact participating Virginia banks to apply for this assistance.
<u><i>Economic Development Loan Fund Program</i></u> provides gap financing for working capital and fixed asset financing to new and expanding Virginia businesses that create or save jobs in Virginia, or provide for quality of life in the community. Borrowers can also get loans through the Virginia Defense Conversion Revolving Loan Fund for businesses which have lost a significant amount of defense-related business through military downsizing.	<u><i>Providing Access to Capital for Entrepreneurs (P.A.C.E.) Program</i></u> provides credit enhancements to participating banks through a Capital Access Program or loan guarantees. Currently, the majority of transactions in this Program are for capital access loans.
<u><i>Small Business Environmental Compliance Assistance Fund</i></u> is a revolving loan program for small businesses that need equipment to comply with the Clean Air Act or for voluntary pollution prevention.	<u><i>Industrial Development Bond Program</i></u> is a financing vehicle in which the Authority is a conduit issuer of tax-exempt and taxable industrial development bonds for qualifying Virginia businesses and 501(c)3 entities.

<u>Virginia Capital Access Program (VCAP or Virginia Small Business Growth Fund)</u> encourages banks to lend to small businesses by providing a matching reserve to the bank to offset default losses.	<u>Southside Tobacco Region Capital Access Program (TCAP)</u> is a program very similar to the VCAP program, with the exception that it provides assistance to small businesses located within the Southside Tobacco Region.
<u>Virginia Community Reinvestment Program</u> is a new program for fiscal year 2006. This program is designed to provide funding for businesses or 501(c)3 entities to expand, improve, or acquire real estate or machinery, provided the entities are located within certain geographic areas, if the owner is a member of certain disadvantaged groups, or is shown to directly impact quality of life initiatives. There was no activity within this program during fiscal year 2006.	<u>New Markets Tax Credits Program</u> is the other new program in fiscal year 2006. The program operates in much the same fashion as the Virginia Community Reinvestment Program, and seeks to attract or expand business opportunities within certain qualified active low-income communities. There was no activity within this program during fiscal year 2006.

The Authority derives operating income from interest earned on loans receivable, application and bond fees, and any recovery of loans previously charged off. Non-operating income consists of securities lending and interest earned from investments. The Authority maintains the majority of its cash with the Treasurer of Virginia. Operating expenses include loan write-offs, matching enrollment fees for the capital access programs, personal services, and contractual services. The Authority's expenses exceeded revenues primarily due to \$258,526 in Grants and Distributions to Localities, which is activity from the Virginia Capital Access Program. The following is a summary of financial activity for the major programs within the Authority.

Assets and Liabilities for Fiscal Year 2006

Assets:

Economic Development Loan Fund Program	\$17,918,217
Child Care Financing Program	3,585,653
Loan Guaranty Program	2,743,805
Virginia Capital Access Program	2,421,882
Small Business Environmental Compliance Assistance Fund	931,398
Southside Tobacco Region Capital Access Program	727,944
Providing Access to capital for Entrepreneurs (PACE) Program	315,529
Total	<u>28,644,428</u>

Liabilities:

Economic Development Loan Fund Program	2,023,141
Loan Guaranty Program	45
Virginia Capital Access Program	2,419,781
Small Business Environmental Compliance Assistance Fund	61,197
Southside Tobacco Region Capital Access Program	571,333
Providing Access to capital for Entrepreneurs (PACE) Program	88,211
Total	<u>\$ 5,163,708</u>

Revenues, Expenses, and Operating Income for Fiscal Year 2006

	Economic Development Loan Fund Program	Loan Guaranty Program	Child Care Financing Program	Small Business Environmental Compliance Assistance Fund	Virginia Capital Access Program	Southside Tobacco Region Capital Access Program	P.A.C.E. Program	Total
Revenues:	<u>\$471,121</u>	<u>\$92,094</u>	<u>\$98,350</u>	<u>\$ 22,886</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$684,451</u>
Expenses:								
Personal services	114,724	-	39,468	92,165	-	-	-	246,357
Contractual services	1,077	6,182	427	1,071	-	-	-	8,757
Grants and disbursements to localities	-	-	-	2,934	258,526	50,000		311,460
Other expenses	<u>143,036</u>	<u>733</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>57,246</u>	<u>-</u>	<u>201,015</u>
Total expenses	<u>258,837</u>	<u>6,915</u>	<u>39,895</u>	<u>96,170</u>	<u>258,526</u>	<u>107,246</u>	<u>-</u>	<u>767,589</u>
Operating income/(loss)	<u>\$212,284</u>	<u>\$85,179</u>	<u>\$58,455</u>	<u>\$(73,284)</u>	<u>\$(258,526)</u>	<u>\$(107,246)</u>	<u>\$ -</u>	<u>\$(83,138)</u>



Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts

P.O. Box 1295

Richmond, Virginia 23218

April 19, 2006

The Honorable Timothy M. Kaine
Governor of Virginia
State Capital
Richmond, Virginia

The Honorable Thomas K. Norment, Jr.
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

We have audited the financial records and operations of the **Virginia Small Business Finance Authority** (Authority) for the year ended June 30, 2006. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions on the Commonwealth Accounting and Reporting System and other Authority financial records, review the adequacy of the Authority's internal controls, and test compliance with applicable laws and regulations.

Audit Scope and Methodology

The Authority's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Loan Programs	Payroll expenditures
Cash	Expenditures

We performed audit tests to determine whether the Authority's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel; inspection of documents, records, and contracts; and observation of the Authority's operations. We tested transactions and performed analytical procedures. We also confirmed bank balances with outside parties.

Conclusions

We found that the Virginia Small Business Financing Authority properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Authority records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System and other Authority financial records.

We noted no matters involving internal control and its operation that we consider necessary to be reported to management. The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Exit Conference

We discussed this report with management April 19, 2007.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.



AUDITOR OF PUBLIC ACCOUNTS

TAS:sks
sks:

AUTHORITY OFFICIALS

VIRGINIA SMALL BUSINESS FINANCE AUTHORITY

Scott Parsons, Executive Director

BOARD MEMBERS

Andrew Brownstein, Chairman

Hattie Hamlin, Vice Chairman

Jane-Scott Cantus	Michael Joyce
James Chang	Leon Moore
Jeffrey Jones	Pallabi Saboo

John Stephens

Braxton Powell, ex-officio voting member

Louisa Strayhorn, ex-officio voting member

Stacy Burrs, ex-officio non-voting member

A. Carole Pratt, ex-officio non-voting member

Scott Parsons, Secretary and Treasurer