

**VIRGINIA SMALL BUSINESS FINANCING AUTHORITY**

**REPORT ON AUDIT  
FOR THE YEAR ENDED  
JUNE 30, 2007**



## **AUDIT SUMMARY**

Our audit of the Virginia Small Business Financing Authority for the year ended June 30, 2007, found:

- 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 Financing Authority provides Virginia's businesses access to capital through financing programs 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.

The following chart highlights the various programs administered by the Authority.

<u><i>Economic Development Loan Fund Program</i></u> provides loans to new and expanding Virginia businesses that create or save jobs in Virginia, or provide economic and "quality of life" development 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>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>State Direct Loan Program</i></u> is a new program in fiscal year 2007. This loan program provides access to capital to new and existing small businesses and economic development authorities for a variety of purposes. The program operates much like the Economic Development Loan Fund, but without the geographical restrictions.	<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>Virginia Capital Access Program (VCAP or Virginia Small Business Growth Fund)</i></u> encourages banks to lend to small businesses by providing a matching reserve to the bank to offset default losses.	<u><i>Southside Tobacco Region Capital Access Program (TCAP)</i></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><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>Loan Guaranty Program</i></u> provides participating local banks deficiency loan guarantees for loans made to Virginia businesses that do not qualify for conventional bank financing. Borrowers contact participating Virginia banks to apply for this assistance.
<u><i>Industrial Development Bonding Program</i></u> is a financing vehicle in which the Authority is conduit issuer of tax exempt and taxable industrial development bonds for qualifying Virginia businesses and 501(c) 3 entities.	

The Authority provides direct and indirect lending through the programs described above. The direct lending programs provide loans directly to Virginia businesses, or economic development authorities and localities. The indirect lending programs provide either loan guarantees to commercial banks to increase access to capital for businesses or provide a matching reserve to banks lending to small businesses. The Authority is also the statewide conduit issuer of tax-exempt industrial development bonds for manufacturers and 501(c) 3 organizations.

The default rate of these programs vary from as low as zero, for the State Direct Loan program which began during fiscal year 2007, to as high as 5.5 percent for the Economic Development Loan Fund program. Due to the type of borrower and nature of the loans, current national economic conditions do not greatly affect the Authority's direct loan programs. In addition, the indirect programs have not had any significant changes in losses since the national economy has slowed.

The following table details the cash and receivables of the direct financing programs at June 30, 2007:

	<u>Direct Financing Programs at June 30, 2007</u>			
	<u>State Direct Loan Program</u>	<u>Child Care Financing Program</u>	<u>Economic Development Loan Fund Program</u>	<u>Small Business Environmental Compliance Assistance Fund</u>
Cash	\$ 9,306	\$1,975,663	\$9,784,497	\$132,755
Receivables (Net)	\$746,785	\$1,711,294	\$6,359,820	\$793,261
Default rate since inception	0.0%	3.0%	5.5%	2.9%
Number of Loans Outstanding	1	56	18	24

The following table outlines the cash and restricted assets of the indirect financing programs. The amounts in the restricted loan loss reserve represent the fees provided by the Authority and the borrower.

	<u>Indirect Financing Programs at June 30, 2007</u>			
	<u>Loan Guaranty Program</u>	<u>P.A.C.E. Program</u>	<u>VCAP</u>	<u>TCAP</u>
Cash	\$3,273,471	\$174,382	\$ 191,082	\$115,111
Restricted Loan Loss Reserve				
Accounts	\$ -	\$108,435	\$2,521,430	\$600,396
Default rate since inception	1.9%	5.2%	3.2%	0.0%

Due to the small size of the portfolios, the Authority does not make allowances for bad debts. The direct loan programs writes off all or part of the debt after a 90 to 120 day delinquency occurs and the Authority anticipates a likely loss. The indirect loan programs put the loan loss fee into the reserve accounts; therefore, as the economy changes, the Authority does not anticipate any addition financial impact. The Loan Guarantee Program is the exception and reserves eight percent of each loan.

The following table outlines the Authority's revenues, expenses, and income for fiscal year 2007. Fifty percent of the Authority's revenues come from interest earnings on cash in various accounts. An additional 30 percent comes from the interest earnings on outstanding loans.

The majority of the transfers listed below relate to \$1.25 million in General Fund appropriations (\$750 thousand to the State Direct Loan program and \$500 thousand to the VCAP program). In addition, there was a \$133,000 repayment between the VCAP fund and the Loan Guaranty program. The VCAP fund borrowed these funds during fiscal year 2006 to keep the VACP program operational.

Revenues, Expenses, and Income for Fiscal Year 2007

	<u>Direct Loan Programs</u>			Small Business Environmental Compliance Assistance Fund
	<u>State Direct Loan Program</u>	<u>Child Care Financing Program</u>	<u>Economic Development Loan Fund</u>	
Revenues:				
Interest on loans	\$ 7,122	\$77,655	\$314,110	\$21,639
Non-operating interest	-	73,533	407,481	8,230
Fees	-	-	500	60
Other	<u>-</u>	<u>6,262</u>	<u>15,155</u>	<u>191</u>
Total revenues	<u>7,122</u>	<u>157,450</u>	<u>737,246</u>	<u>30,120</u>
Expenses:				
Personal services	-	93,069	130,932	50,162
Contractual services	-	70	12,005	-
Grants and distributions to localities	-	-	-	-
Loan charge off	<u>-</u>	<u>906</u>	<u>322,781</u>	<u>-</u>
Total expenses	<u>-</u>	<u>94,045</u>	<u>465,718</u>	<u>50,162</u>
Net income before transfers	7,122	63,405	271,528	(20,042)
Transfers	<u>750,000</u>	<u>-</u>	<u>-</u>	<u>77,246</u>
Total net income	<u>\$757,122</u>	<u>\$63,405</u>	<u>\$271,528</u>	<u>\$57,204</u>

	<u>Indirect Loan Programs</u>				
	<u>Loan Guaranty Program</u>	<u>P.A.C.E. Program</u>	<u>VCAP</u>	<u>TCAP</u>	<u>Total Programs</u>
Revenues:					
Interest on loans	\$ -	\$ -	\$ -	\$ -	\$ 420,526
Non-operating interest	197,142	9,955	19,886	-	716,227
Fees	225,830	731	-	-	227,121
Other	<u>-</u>	<u>92</u>	<u>39,484</u>	<u>-</u>	<u>61,184</u>
Total revenues	<u>422,972</u>	<u>10,778</u>	<u>59,370</u>	<u>-</u>	<u>1,425,058</u>
Expenses:					
Personal services	-	-	-	41,500	315,663
Contractual services	26,372	-	-	-	38,447
Grants and distributions to localities	-	63,714	237,389	-	301,103
Loan charge off	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>323,687</u>
Total expenses	<u>26,372</u>	<u>63,714</u>	<u>237,389</u>	<u>41,500</u>	<u>978,900</u>
Net income before transfers	396,600	(52,936)	(178,019)	(41,500)	446,158
Transfers	<u>133,000</u>	<u>-</u>	<u>367,000</u>	<u>-</u>	<u>1,327,246</u>
Total net income	<u>\$529,600</u>	<u>\$(52,936)</u>	<u>\$188,981</u>	<u>\$(41,500)</u>	<u>\$1,773,404</u>



# Commonwealth of Virginia

**Walter J. Kucharski, Auditor**

**Auditor of Public Accounts  
P.O. Box 1295  
Richmond, Virginia 23218**

May 21, 2008

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

The Honorable M. Kirkland Cox  
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 Financing Authority** (Authority) for the year ended June 30, 2007. We conducted this performance audit in accordance with generally accepted Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## 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
- Cash
- Expenses
- Payroll



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 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 and Report Distribution

We discussed this report with management on June 11, 2008.

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/wdh

## AUTHORITY OFFICIALS

### VIRGINIA SMALL BUSINESS FINANCING AUTHORITY

Scott Parsons, Executive Director

## BOARD MEMBERS

Andrew Brownstein, Chairman

Hattie Hamlin, Vice Chairman

George Bryan	Jane-Scott Cantus
Michael Joyce	Jeffrey Jones
Leon Moore	Jack Stephens

Pallabi Saboo

Braxton Powell, ex-officio voting member

Lynda Sharp Anderson, ex-officio voting member

Robert B. Nealon, ex-officio non-voting member

Scott Parsons, Secretary and Treasurer