

## **AUDIT SUMMARY**

Our audit of the Virginia Small Business Financing Authority for the year ended June 30, 1999, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System and in the Authority's financial accounting records;
- no material weaknesses in internal control;
- no instances of noncompliance that are required to be reported; and
- adequate implementation of corrective action on the prior year audit finding.

December 30, 1999

The Honorable James S. Gilmore, III  
Governor of Virginia  
State Capitol  
Richmond Virginia

The Honorable Richard J. Holland  
Chairman, Joint Legislative Audit  
and Review Commission  
General Assembly Building  
Richmond, Virginia

### INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Virginia Small Business Financing Authority** (Authority) for the year ended June 30, 1999. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

#### Audit Objectives, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Authority's accounting records, review the adequacy of the Authority's internal control, and test compliance with applicable laws and regulations. We also reviewed the Authority's corrective actions of audit findings from prior year reports.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Authority's operations. We also tested transactions and performed such other auditing procedures as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Revenues	Expenditures
Federal Compliance	

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. 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.

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.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

### Audit Conclusions

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

We noted no matters involving internal control and its operation that we consider to be material weaknesses. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to financial operations may occur and not be detected promptly by employees in the normal course of performing their duties.

The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

The Authority has taken adequate corrective action with respect to audit findings reported in the prior year.

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

### EXIT CONFERENCE

We discussed this report with management at an exit conference held on February 14, 2000.

AUDITOR OF PUBLIC ACCOUNTS

## AGENCY HIGHLIGHTS

The Virginia Small Business Financing Authority (Authority) provides financial assistance to small businesses in the Commonwealth by providing loans, guarantees, insurance, and other assistance, thereby encouraging the investment of private capital in small business. The Authority issues industrial development bonds and guarantees small business loans for banks.

The Authority's operating revenue and expenses during fiscal year 1999 were \$698,976 and \$623,431, respectively. Significant revenue collections included interest and other investment income, industrial development bond fees, and loan guarantee fees. The Authority's expenses consisted primarily of contractual services, payroll, and fringe benefits. The Authority invests excess cash in the Local Government Investment Pool (LGIP), as well as participates in the Securities Lending Program. Investments totaled \$4,171,000 at June 30, 1999.

The Director of the Department of Business Assistance appoints the Authority's Executive Director. Further, the Department provides office space and pays certain administrative expenses, including the Executive Director's salary.

### Economic Development Revolving Loans

The Virginia Economic Development Revolving Loan Fund provides loans to small companies to bridge the gap between private debt financing and private equity. The Virginia Defense Conversion Revolving Loan Fund provides loans to defense-dependent companies seeking to diversify and expand into commercial markets. At June 30, 1999, the Economic Development Revolving Loan Fund had loans outstanding totaling \$783,091 and a cash balance of \$11,407,670. The Defense Conversion Revolving Loan Fund had loans outstanding in the amount of \$4,606,411 and a cash balance of \$7,321,576. Defaulted loans for the Revolving Loan Funds amounted to \$1,938,556 since inception. The Authority works with a law firm, assigned by the Attorney General's office, to pursue collection of defaulted loans.

In December 1998, the Authority sold outstanding loans totaling \$12,102,052 from the Economic Development and the Defense Conversion Revolving Loan Funds. The Authority plans to increase marketing efforts and issue new loans with proceeds from the sale.

### Loan Guarantees

The Authority guarantees loans made to small businesses by banks. At June 30, 1999, the Authority had outstanding loan guarantees totaling \$636,280. The Authority maintains an 8 percent outstanding loan balance as a loan loss reserve. The loan loss reserve was \$50,902 at fiscal year end. If a loan goes into default, the Authority uses funds in the loan loss reserve to cover the guarantee. Lending banks pursue collection of loans in default. The Authority receives a portion of any recovered funds as reimbursement on the loan guarantee paid to the bank. Historically, the loan default rate has been 4.6 percent and defaults since inception have amounted to \$427,150.

### Child Care and Development

The Authority manages a portion of the Child Care and Development Block Grant by providing the Child Day Care Financing Program. The Authority takes applications, approves and makes direct loans, develops and implements marketing programs, and provides oversight and supervision to the manager of the

loan program. At June 30, 1999, the Authority had loans outstanding of \$1,496,045. Delinquent loans for the program amounted to \$80,817. The Authority works with the Attorney General's office to pursue collection of any defaulted loans. The Authority receives reimbursement for operating expenses for the administration of the program.