

"as listed on the following page" or "as listed in the accompanying index").

iii. In addition to expressing an opinion on the basic financial statements (the statement of financial position, statement of operations realized and statement of cash flows), the accountant must express an opinion on the supplementary financial information. The supplementary information should be addressed in a separate paragraph of the Independent Auditors' Report. As with the basic financial statements, the supplementary statements and schedules may be listed in the report itself or listed separately and referred to in the report.

iv. Almost all SBICs have Loans and Investments, the value of which must be estimated by the Board of Directors or General Partner(s) in the absence of readily ascertainable market values. The auditor's reports for such SBICs must include an explanatory paragraph addressing portfolio valuations, in which the auditor states whether the valuation procedures are reasonable and the underlying documentation is appropriate. It is no longer acceptable to state that valuations involve subjective judgment which is not susceptible to substantiation by auditing procedures. The paragraph should follow the AICPA's reporting recommendations presented in chapter 9 of "Audits of Investment Companies".

V. Sample Report. Following is a sample Independent Auditors' Report which is acceptable to SBA, based on generally accepted auditing standards in effect as of the publication date of these regulations. Any subsequent changes in generally accepted auditing standards which affect reporting requirements must be reflected in the Independent Auditors' Report included in a Licensee's filing of SBA Form 468, regardless of whether or not SBA has published an updated sample report.

Independent Auditors' Report

The Board of Directors of [Licensee]

or

The General Partner(s) and Limited Partners of [Licensee]

We have audited the statement of financial position of [Licensee] as of [closing date of fiscal year] and the related statements of operations realized and cash flows for the year then ended included in SBA Form 468. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of [Licensee] as of [closing date of fiscal year], and the results of its operations and cash flows for the year then ended in conformity with generally accepted accounting principles.

As explained in Note _____, the financial statements include investments valued at \$_____ as of [closing date of fiscal year], whose values have been estimated by the [Board of Directors] [General Partner(s)], in the absence of readily ascertainable market values. We have reviewed the procedures used by the [Board of Directors] [General Partner(s)] in arriving at its estimates of value of such investments and have inspected underlying documentation, and, in the circumstances, we believe the procedures are reasonable and the documentation appropriate. However, because of the inherent uncertainty of valuation, those estimated values may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information contained in the [analysis of stockholders' equity] [analysis of partners' capital], computations of retained earnings available for distribution and of regulatory and leverageable capital, schedules of commitments and guarantees, and schedules 1 through 7 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

C. Access to Accountants' Working Papers

At its discretion, SBA may assign its examiners or other personnel to review the accountant's working papers. The audit engagement agreement between the Licensee and the IPA shall provide that the accountant's working papers will be made available for review upon request of the SBA.

D. Accountants' Responsibility for Valuations

i. The investment portfolios of virtually all SBICs contain nonmarketable securities, the values of which must be estimated in the absence of readily ascertainable market values. It is the responsibility of the Board of Directors or the General Partner(s) to estimate the value of such securities in good faith.

ii. The IPA does not act as an appraiser for security values estimated by the Board of Directors or General Partner(s), and is not expected to perform an audit of the portfolio concerns. The IPA's review of a Licensee's portfolio valuations shall address the following questions:

- (1) Does the Licensee have a written valuation policy which has been approved by SBA?
- (2) Do the Licensee's valuations of its portfolio concerns reflect consistent adherence to its valuation policy?

(3) Has the Licensee documented the basis for its valuations, and does such documentation indicate that a reasonable analysis of available information has been performed?

iii. Based upon the auditing procedures performed, the IPA shall express an opinion as to whether the Licensee's valuation procedures are reasonable and the documentation is appropriate.

iv. SBA requirements concerning portfolio valuations are set forth in Appendix II to Part 107. Appendix II contains recommended valuation techniques for securities of various types, as well as requirements concerning written valuation policy, frequency of valuation, and documentation. A Licensee has the option of adopting the model valuation policy included in Appendix II or obtaining SBA approval of an alternative valuation policy.

v. In addition to the SBA valuation requirements, IPAs may also wish to review SEC Accounting Series Release No. 118 (section 404.03, "Codification of Financial Reporting Policies").

vi. The IPA shall test a sufficient number of valuations to support an opinion. Testing of valuations representing less than 50 percent of the value of the entire portfolio shall be presumed to be insufficient to support an opinion.

vii. If the audit discloses that the valuation procedures are inadequate, unreasonable or inconsistent with the Licensee's valuation policy, or that the underlying documentation does not adequately support the valuations, the IPA's opinion shall be modified to indicate a lack of conformity with generally accepted accounting principles. The opinion may be qualified (using the phrase "except for") or, depending upon the possibility of a material misstatement, the accountant may determine that an adverse opinion is appropriate.

E. Audit Adjustments

All audit adjustments shall be entered in the Licensee's records before issuance of the Independent Auditors' Report. As a result, the financial statements accompanying the report will agree with the books as adjusted as of the statement date, giving consideration to reclassification of account balances for report purposes. If the adjustments are not so recorded on the Licensee's books, a statement shall be made by the IPA to this effect.

F. Reporting Irregularities

i. *Reporting Irregularities and Illegal Acts to SBA.* An independent public accountant that detects irregularities or illegal acts individually or collectively material to the financial statements, or irregularities or illegal acts relative to SBA programs whether or not material, shall advise management in writing. Management, in turn, shall immediately advise, in writing, the Associate Administrator for Investment, Investment Division, 409 Third Street, SW, Washington, DC 20416. Management, in advising SBA, shall, to the extent practicable, describe the irregularities or illegal acts and their effects on the financial statements and SBA programs. Auditors shall determine whether management reported the irregularities or