

# Financial Reporting



## SUCCESS STORY: Family Business Blends Old World Tastes with New World Innovation

Anita's Mexican Food Corporation,  
San Bernardino, California

Anita's Mexican Food Corporation is a wholesale food manufacturer and co-packer. The company's origins date back to 1958 when patriarch Mauro Robles came from Mexico, earned citizenship, and sought to create new products that respected Old World tastes and traditions. Co-owners **Ricardo Robles, Pablo "Rene" Robles,** and **Jackie Robles** are SBA's *2014 California Small Business Persons of the Year*. They were nominated in recognition of their accomplishments in growing revenues, 112 percent over the past three years, and increasing employment by 129 positions.

What began as a flour tortilla manufacturer grew to become a major flour- and corn-based food manufacturing wholesaler and co-packer with more than 1,000 different products under eight trademarks. It specializes in tortilla and snack foods distributed nationally and internationally to Canada, South Korea, New Zealand, and throughout South America. Anita's Mexican Food Corporation was the first company to introduce organic corn tortilla chips in various types of organic corn. After a national firm flooded the market, the business innovated to become the first company in the organic, GMO-free, and gluten-free corn tortilla chip market. The company also operates a flour tortilla manufacturing facility in East Los Angeles, one of the largest employers in its area that produces more than 1.5 million tortillas a day.

Through 504 loan financing, the business completed a project that totaled over \$9.7 million for real estate, improvements, and equipment.



## MESSAGE FROM THE CHIEF FINANCIAL OFFICER

November 17, 2014

I am pleased to submit the U.S. Small Business Administration's (SBA) Agency Financial Report for fiscal year 2014. An independent audit has earned the SBA an unmodified opinion with no material weaknesses.

The auditor identified one instance of non-compliance with applicable laws and regulations as of September 30, 2014. Due to ongoing technology challenges with the Agency's legacy mainframe information system, not all co-borrowers and guarantors and disaster charged-off loans were referred to the Treasury for cross-servicing collection of debt as required by the Debt Collection Improvement Act. Improvements in technology and processes continue to be implemented to support compliance on the referral of loans, and the SBA will make system modifications in accordance with an Agency plan to resolve the completeness and accuracy of referrals to Treasury.

Improvements continue to be made in the integration and operation of the Acquisition Division. In FY 2014, CFO staff met with each program office to develop an advanced acquisition strategy that coordinates procurement actions and budgetary requirements. These sessions proved particularly important to assist managers in navigating the FY 2014 continuing resolution budgets that segmented annual budgetary allocations. The SBA's acquisition planning has matured significantly through this collaborative process, and communication with program offices has greatly improved. By integrating the budget and acquisition process, program managers are better able to plan and execute. Throughout 2014, SBA's Acquisition Division has made considerable progress toward standardizing and improving SBA's procurement process. The SBA exceeded its overall FY 2014 small business contracting goal of 68 percent—the highest percentage goal in the government for small business contracts – as well as all socio-economic sub-goals. The SBA also received a procurement scorecard grade of "A" for the Agency's FY 2013 acquisition achievements.

The CFO's office also made great strides in the reduction of improper payments for disbursement for goods and services in FY 2014. The improper payment rate dropped by more than 3 percent to the current year rate of 8.4 percent. This year's rate brings the Agency below the mandatory compliance level.

A major challenge to SBA operations was the federal civilian government shutdown early in the fiscal year. SBA executed contingency operation plans to facilitate a smooth transition from one fiscal year to the next with a limited group of excepted employees. Despite this initial setback, the CFO's office continued to drive the Agency towards excellence in resource management by synchronizing budget, acquisition, and performance information to provide decision makers with the information they need to effectively execute Agency programs.

Another major process improvement has been SBA's implementation of the Quick Pay initiative to ensure the timely payment of invoices to prime contractors. I am proud to say that these process improvements resulted in more than \$110 million in accelerated payments to SBA contractors during the June 2013 to July 2014 period.

The SBA continued its efforts to reduce Agency-wide spending on non-disaster travel in FY 2014 to comply with the President's Campaign to Cut Waste. Travel spending caps were set for each office, placing priority on mandatory and compliance trips. Through careful planning and management, the Agency was able to stay within its mandated travel cap.

This year, the SBA published its FY 2014-2018 Strategic Plan to guide the Agency over the next five years. The plan includes three strategic goals that focus on job growth and creation, small business advocacy, and effective internal management and risk mitigation. The strategic goals help guide the Agency's resource and management decisions. Each strategic goal contains objectives which are directly tied to performance both at the individual level and Agency-wide. This framework is essential to ensure that the SBA continues to play a key role in strengthening America's economy by providing tools to help grow businesses and create jobs.

For the eighth straight year the SBA has won the Certificate of Excellence in Accountability Reporting (CEAR) award. This award, presented by the Association of Government Accountants, is made to federal agencies following a rigorous, independent review against established standards for presentation. The award recognizes high-quality agency financial and performance reports that effectively illustrate and assess financial and program performance, accomplishments and challenges, cost and accountability. CFO Managers and staff work diligently to provide meaningful and high quality reporting information on behalf of the Agency, and the CEAR award is recognition of their efforts.

I also want to recognize the independent Audit and Financial Management Advisory Committee who, since 2004, has advised us in the financial reporting process and audit cycle, and made recommendations pertaining to our financial statement footnotes and the AFR prior to publication. I thank them for their support and dedication to continued improvement.

SBA's efforts to assist entrepreneurs and small business owners are especially critical to a healthy economy. Throughout America's history, small businesses have played the leading role in job creation. In fact, more than half of working Americans own or work for a small business and small businesses are responsible for two out of every three net new private sector jobs created over the past decade. My office is proud to be a part of this effort.

Sincerely,



Tami Perriello  
Associate Administrator for Performance Management  
and Chief Financial Officer (Acting)

## AUDIT AND FINANCIAL MANAGEMENT ADVISORY COMMITTEE'S REPORT

The Audit and Financial Management Advisory Committee (the Committee) assists the Administrator in overseeing the U.S. Small Business Administration's (SBA's) financial operations. As part of that responsibility, the Committee meets with Agency management, the Agency's Inspector General, and its external auditors to review and discuss SBA's external financial audit coverage, the effectiveness of SBA's internal controls over its financial operations, and its compliance with certain laws and regulations that could materially impact SBA's financial statements. SBA's external auditors are responsible for expressing an opinion on the conformity of SBA's audited financial statements with the U.S. generally accepted accounting principles. The Committee reviews the findings of the Inspector General and external auditors, and SBA's responses to those findings, to ensure that SBA's plan for corrective action includes appropriate and timely follow-up measures. In addition, the Committee reviews the draft Agency Financial Report (AFR), including its financial statements, and provides comments to management who has primary responsibility for the AFR. The Committee met formally once during the year and once via telecom with respect to these responsibilities on FY 2014 financial management and reporting. During the formal meeting the Committee met with the Inspector General and external auditors without SBA management being present and discussed with the external auditors the matters that are required to be discussed by generally accepted auditing standards. Nothing came to our attention as a result of these discussions to indicate changes were needed to the financial statements and notes thereto that are included in the FY 2014 AFR.



Edward J. Mazur  
Chairman  
Audit and Financial Management Advisory Committee

## INSPECTOR GENERAL'S AUDIT REPORT



U.S. SMALL BUSINESS ADMINISTRATION  
OFFICE OF INSPECTOR GENERAL  
WASHINGTON, D.C. 20416

TRANSMITTAL MEMORANDUM  
Report No. 15-02

**Date:** November 17, 2014

**To:** Tami Perriello  
Acting Chief Financial Officer

**From:** Troy M. Meyer   
Assistant Inspector General for Auditing

**Subject:** *Independent Auditors' Report on the SBA's FY 2014 Financial Statements*

We contracted with the independent certified public accounting firm KPMG LLP (KPMG) to audit the U.S. Small Business Administration's (SBA) consolidated financial statements for fiscal year (FY) 2014, ending September 30, 2014. This audit is an annual requirement of the Chief Financial Officers Act of 1990, and was conducted in accordance with the *Generally Accepted Government Auditing Standards*; the Office of Management and Budget Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements*; and the U.S. Government Accountability Office's *Financial Audit Manual* and *Federal Information System Controls Audit Manual*.

The attached independent auditor's report presents an unmodified opinion on the SBA's consolidated financial statements for FY 2014. Specifically, KPMG reported that:

- The financial statements were fairly presented in all material aspects in conformity with U.S. generally accepted accounting principles.
- There were no material weaknesses in internal control.
- There is a significant deficiency related to the SBA's information technology security controls, which has been identified in the past.
- There is one instance of noncompliance with laws and regulations related to the Debt Collection Improvement Act of 1996, which also has been reported in the past.

Details regarding KPMG's conclusions are included in the "Compliance and Other Matters" section, and Exhibits I and II to this report. Within 30 days of this report, KPMG expects to issue a separate letter to SBA management regarding other, less significant matters that came to its attention during the audit.

We reviewed a copy of KPMG's report and related documentation and made necessary inquiries of their respective representatives. Our review was not intended to enable us to express—and we do not express—an opinion on the SBA's financial statements, KPMG's conclusions about the effectiveness of internal controls, or its conclusions about the SBA's compliance with laws and regulations. However, our review disclosed no instances where KPMG did not comply, in all material respects, with the *Generally Accepted Government Auditing Standards*.

We provided a draft of KPMG's report to the SBA's Acting Chief Financial Officer, who concurred with its findings and recommendations and agreed to implement the recommendations. The Acting Chief Financial Officer's comments are attached as Exhibit III to this report.

We appreciate the cooperation and assistance of the SBA and KPMG. Should you or your staff have any questions, please contact me at (202) 205-7390 or Jeffrey R. Brindle, Director, Information Technology and Financial Management Group at (202) 205-7490.

Attachment

## INDEPENDENT AUDITORS' REPORT ON FY 2014 FINANCIAL STATEMENTS



**KPMG LLP**  
 Suite 12000  
 1801 K Street, NW  
 Washington, DC 20006

### Independent Auditors' Report

Inspector General  
 United States Small Business Administration:

#### Report on the Financial Statements

We have audited the accompanying consolidated financial statements of the U.S. Small Business Administration (SBA), which comprise the consolidated balance sheets as of September 30, 2014 and 2013, and the related consolidated statements of net cost, and changes in net position, and combined statements of budgetary resources for the years then ended, and the related notes to the consolidated financial statements.

#### *Management's Responsibility for the Financial Statements*

The SBA's management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditors' Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 14-02, require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

KPMG LLP is a Delaware limited liability partnership, the U.S. member firm of KPMG International Cooperative ("KPMG International"), a Swiss entity.



### ***Opinion on the Financial Statements***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Small Business Administration as of September 30, 2014 and 2013, and its net costs, changes in net position, and budgetary resources for the years then ended in accordance with U.S. generally accepted accounting principles.

### ***Other Matters***

#### ***Required Supplementary Information***

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis, Required Supplementary Information, and Required Supplementary Stewardship Information sections be presented to supplement the basic consolidated financial statements. Such information, although not a part of the basic consolidated financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the basic consolidated financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic consolidated financial statements, and other knowledge we obtained during our audits of the basic consolidated financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

#### ***Other Information***

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements as a whole. The Message from the Administrator, Other Information, and the information on pages 35 to 39 of the *Agency Financial Report*, are presented for purposes of additional analysis and are not a required part of the basic consolidated financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

### **Other Reporting Required by *Government Auditing Standards***

#### ***Internal Control Over Financial Reporting***

In planning and performing our audit of the consolidated financial statements as of and for the year ended September 30, 2014, we considered the SBA's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the SBA's internal control. Accordingly, we do not express an opinion on the effectiveness of the SBA's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.



Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, we did identify a combination of certain deficiencies in internal control, described in Exhibit I, that we consider to be a significant deficiency.

#### ***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether SBA's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 14-02. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 14-02. Specifically, our audit results noted a noncompliance with the *Debt Collection Improvement Act of 1996*. Further details of the noncompliance are described in Exhibit II.

We also performed tests of its compliance with certain provisions referred to in Section 803(a) of the *Federal Financial Management Improvement Act of 1996* (FFMIA). Providing an opinion on compliance with FFMIA was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of FFMIA disclosed no instances in which the SBA's financial management systems did not substantially comply with the (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level.

#### ***SBA's Response(s) to Findings***

The SBA's response to the findings identified in our audit is described in the accompanying Exhibit III. The SBA's response was not subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we express no opinion on the response.

#### ***Purpose of the Other Reporting Required by Government Auditing Standards***

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the SBA's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Washington, DC  
November 17, 2014

## Exhibit I

## U.S. Small Business Administration

## Significant Deficiency

*Improvement Needed in Information Technology Security Controls*

During the FY 2014 financial statement audit, we found that the U.S. Small Business Administration (SBA) implemented corrective actions on some of the prior year findings; however, a number of conditions persisted in FY 2014 that reduced SBA's ability to effectively manage its information system risk. As a result, collectively, these conditions present a significant deficiency in SBA's internal control environment.

In an effort to provide additional clarity to SBA management with respect to the corrective actions required, we enhanced our prior year recommendations where issues persisted in FY 2014, and issued additional recommendations for the new control deficiencies identified. In the sections below, we distinguish between recurring conditions and related recommendations, and those that were newly identified in FY 2014. We have omitted some technical details from the conditions and recommendations due to the sensitivity of the information. These details were communicated to management through Notices of Findings and Recommendations throughout the audit.

We have summarized the Information Technology (IT) control deficiencies that we noted during the FY 2014 audit below, and have organized them by the following general IT control objectives: logical and physical access controls, application change management, system configuration management, and contingency planning.

*Logical and Physical Access Controls*

An integral part of the effectiveness of an organization's security program management efforts should be to ensure that logical and physical access controls provide reasonable assurance that IT resources, such as data files, application programs, and IT-related facilities/equipment, are protected against unauthorized modification, disclosure, loss, or impairment.

Our audit found that the following control deficiencies identified in the prior year(s) persisted in FY 2014:

- User accounts to the network and some financial systems were not properly authorized.
- User accounts to the network and some financial systems were not recertified in accordance with SBA policy.
- The principle of "least privilege" for user/service accounts with network administrator privileges was not enforced.
- User accounts to the network and some financial systems were not disabled or removed promptly upon personnel termination.
- The employee exit clearance and contractor off-boarding processes were not standardized to ensure that access to SBA's network and financial systems was timely removed upon separation.
- Security settings for the network were not enforced for all organizational units.
- Processes for consistently and effectively reviewing audit logs for the network and financial systems were not implemented.
- A process for approving, administering, and reviewing physical access to the Headquarters (HQ) Data Center had not been defined.

### U.S. Small Business Administration

#### Significant Deficiency

- Remote access to SBA information systems was not configured and provisioned in accordance with SBA policy.

In addition to the matters above, we noted the following additional control deficiency during our FY 2014 audit:

- Known password for the network did not meet SBA standards for password strength and complexity.

#### Recommendations – Logical and Physical Access Controls:

We have issued the following recommendations to address the repeat control deficiencies listed in the section above.

We recommend that the Chief Information Officer (CIO) coordinate with SBA program offices to:

1. Implement and monitor procedures to ensure that access is appropriately granted to employees and contractors, consistent with the conditions on their access forms after all approvals have been obtained.
2. Implement procedures to ensure that user access, including user accounts and associated roles, is reviewed on a periodic basis consistent with the nature and risk of the system, and any necessary account modifications be performed when identified. In addition, implement the principle of “least privilege” for user and service accounts.
3. Grant elevated network privileges per business needs only and enforce the concept of least privilege or implement mitigating controls to ensure that activities performed using privileged network accounts (including service accounts) are properly monitored.
4. Improve SBA’s administration of logical system access by taking the following actions:
  - Implement an effective off-boarding process and verify periodically that controls to remove logical access for separated employees from SBA systems are implemented and operating as designed;
  - Establish a process for the identification and removal of separated contractors in order to help ensure that access is timely removed upon contractor separation; and
  - Remove access to the general support systems and major applications (including development and test environments) timely when employees and contractors are terminated.
5. Enforce a network access security baseline(s) across the network that is consistent with SBA’s security policy, Office of Management and Budget directives, and United States Government Configuration Baseline requirements.
6. Improve SBA’s information system logging and auditing program, by taking the following actions:
  - Review and rationalize current audit and logging activities and capabilities to determine their effectiveness in addressing risks to systems and data;
  - Implement and enforce consistent and effective creation of audit records, capturing of relevant auditable events, auditing (i.e., manual or automated review of audit records) for specified

## Exhibit I

## U.S. Small Business Administration

## Significant Deficiency

events, and automated alerting on specified events across SBA's infrastructure using a risk-based approach;

- Retain evidence of the audit log review; and
  - Develop an agency-wide plan and schedule for implementation of the above recommendations.
7. Establish a process to review the list of individuals with HQ data center access permissions periodically, to ensure that only authorized personnel retain access to the HQ data center.
8. Improve SBA's remote access program by taking the following actions:
- Ensure employees acknowledge compliance with security requirements prior to establishing a remote connection to SBA's network when teleworking or otherwise connecting remotely to SBA systems; and
  - Monitor compliance with Standard Operating Procedure (SOP) 90.47.3, *Information System Security Program* and the updated Teleworking SOP.

To address the newly identified logical and physical access control weakness:

We recommend that the CIO:

- 9. Ensure that sensitive passwords meet SBA standards for password strength and complexity.

*Application Change Management*

The integrity of information processing is dependent on the controlled management of changes to the software that controls the processing. Software change management is designed to reduce the risk of unauthorized or erroneous changes of software. Our audit found the following control deficiencies remain, that were identified in a prior year:

- The change management process for some financial applications did not sufficiently reduce the risk of an unauthorized change being made to the production environment. Specifically, the SBA did not review or compare system code to ensure only authorized changes had been made, and the audit log review process was not designed to detect unauthorized changes to application software.
- Segregation of duties were not enforced for one financial application. Additionally, detective controls to mitigate the risk of known segregation of duties issues for two financial applications did not operate for the full fiscal year.
- Required software changes for one financial subsystem were not implemented due to the ongoing code migration project which impacted SBA's compliance with the *Debt Collection Improvement Act of 1996* in that system. This issue was reported as a noncompliance matter in the "Compliance and Other Matters" section of our audit report.

**U.S. Small Business Administration**  
Significant Deficiency

Recommendations – Application Change Management:

We have issued the following recommendations to address the repeat control deficiencies listed in the section above, we recommend that the:

10. Associate Administrator of Capital Access (OCA), in coordination with the CIO, design and implement a combination of preventative and detective controls to address the issues and related risks in the condition above, and ensure an auditable trail of software changes is maintained to prevent and detect unauthorized changes to production programs.
11. Associate Administrator of Disaster Assistance (ODA) and Chief Financial Officer enforce segregation of duties for privileged users or perform mitigating controls to ensure that the risks associated with privileged access remain mitigated.
12. Associate Administrator of the OCA, in conjunction with the CIO, continue to review system protocols to determine if any other coding problems exist that may cause untimely referral of loans, and address outstanding system protocol issues from prior years.

*System Configuration Management*

The primary focus of an organization's system configuration management process should be to control the security configuration of its infrastructure including servers, databases, network equipment, security appliances, and security services. Without such controls, there is a risk that security features could be inadvertently, or deliberately, omitted or turned off, introducing risk into the IT environment.

Our audit noted that the following prior year control deficiency persisted in FY 2014:

- Numerous high- and medium-risk configuration and patch management vulnerabilities were noted in the network and infrastructure supporting certain financial systems.

Recommendations – System Configuration Management:

To address the repeat system configuration management condition above, we recommend that:

13. The CIO coordinate with SBA program offices to address the existing configuration and patch management vulnerabilities noted during our assessment to be in compliance with SBA policy and SBA Vulnerability Assessment Team (VAT) Internal Operating Procedures, Version 1.0. In addition, implement procedures to ensure the consistent implementation and monitoring of SBA approved security configuration baselines across SBA's workstations, servers, databases, network devices, and other security relevant appliances.

*Contingency Planning*

The focus of an organization's contingency planning program should be to provide reasonable assurance that information resources are protected and the risk of unplanned interruptions is minimized. Without such controls, there is a risk that data may be lost or that critical operations may not resume in a timely manner.

Our audit noted that the following prior year control deficiencies persisted in FY 2014:

- An alternate processing site for some financial systems and related support infrastructure had not been established.

**Exhibit I****U.S. Small Business Administration**

## Significant Deficiency

In addition to the matter above, we noted the following additional control deficiency during our FY 2014 audit:

- Full backups for some of the financial systems and related support infrastructure were not retained in accordance with SOP 90.47.3.

**Recommendations – Contingency Planning:**

To address the repeat contingency planning condition above, we recommend that the CIO:

14. Design and implement procedures, resources, and controls to ensure the timely recovery of resources and systems in the event of a disaster or unexpected event.

To address the newly identified contingency planning control weakness, we recommend that the CFO, CIO and Associate Administrator of OCA:

15. Ensure that full backups for financial systems and related support infrastructure are retained in accordance with SBA policies.

**U.S. Small Business Administration**

## Compliance and Other Matters

***Noncompliance with the Debt Collection Improvement Act of 1996***

The *Debt Collection Improvement Act of 1996* (DCIA) assigns the U.S. Department of Treasury (Treasury) the responsibility for collecting delinquent debts, Government-wide. The DCIA requires Federal agencies to transfer their nontax debt over 180 days delinquent to the Treasury. During our testwork over loan charge-offs, we noted the SBA did not refer obligors (i.e., eligible principal borrowers, co-borrowers, and/or guarantors) to the Treasury for offset or cross-servicing at the time of charge-off, as required by the DCIA. Similar instances of noncompliance with the DCIA were reported in prior years. The SBA's noncompliance with the DCIA was the result of both manual errors and deficiencies in information technology controls. For additional discussion of the information technology aspects of this finding, see Exhibit I.

We recommend the Associate Administrator of the Office of Capital Access:

16. Conduct training to educate loan center staff on the proper steps to refer obligors to the Treasury and correct errors after the initial referral.
17. Reinforce the importance of retaining identifying information for all obligors.

## Exhibit III



## CFO Response to Draft Audit Report on FY 2014 Financial Statements

**DATE:** November 17, 2014

**TO:** Troy Meyer, Assistant Inspector General for Auditing

**FROM:** Tami Perriello, Associate Administrator for Performance Management and Chief Financial Officer (Acting) *Tami Perriello*

**SUBJECT:** Draft Audit Report on FY 2014 Financial Statements

The Small Business Administration has received the draft Independent Auditors' Report from KPMG that includes the auditors' opinion on the financial statements and its review of the Agency's internal control over financial reporting and compliance with laws and regulations. The independent audit of the Agency's financial statements and related processes is a core component of SBA's financial management program.

We are pleased that the SBA has again received an unmodified audit opinion from the independent auditor with no material weaknesses. We believe these results accurately reflect the quality of the Agency's financial statements and our improved accounting, budgeting and reporting processes. As you know, the SBA has worked hard in past years to address the findings from our independent auditor. Our core financial reporting data and processes have further improved, and we are proud that the results of our efforts have been confirmed by the independent auditor.

The audit report includes a continuing significant deficiency in SBA's information technology controls. The SBA will continue to work on improvements in IT security. The SBA will track, monitor, and mitigate vulnerabilities in Agency systems. Furthermore, the SBA will clarify and strengthen detailed procedures required to ensure security access controls are in place to protect SBA data from unauthorized modification, disclosure, and loss.

The auditor reported again this year that the SBA is not compliant with the Debt Collection Improvement Act of 1996 related to timely referral of charged-off loans to the Department of the Treasury for its tax refund offset and collection programs. Although the SBA made improvements to correct systemic errors identified last year, the auditors again found instances of charged-off loans where co-borrowers and guarantors were not referred to Treasury. The SBA is working on procedures to correct this issue.

We appreciate all of your efforts and those of your colleagues in the Office of the Inspector General as well as those of KPMG. The independent audit process continues to provide us with new insights and valuable recommendations that will further enhance SBA's financial management practices. We continue to be committed to excellence in financial management and look forward to making more progress in the coming year.

## FINANCIAL STATEMENTS AND NOTES

The U.S. Small Business Administration prepares its financial statements as a critical aspect of ensuring accountability and stewardship for the public resources entrusted to it. Preparation of these statements is also an important part of SBA's financial management goal of providing accurate and reliable information that may be used to assess performance and allocate resources.

SBA's management is responsible for the accuracy and propriety of the information contained in the principal financial statements and the quality of internal controls. The SBA prepares these financial statements from its books and records in accordance with generally accepted accounting principles in the United States as well as formats prescribed by the Office of Management and Budget.

The financial statements include the following reports.

The **Consolidated Balance Sheet** summarizes the assets, liabilities, and net position by major category as of the reporting date. Intragovernmental assets and liabilities resulting from transactions between federal agencies are presented separately from assets and liabilities resulting from transactions with the public.

The **Consolidated Statement of Net Cost** shows, by strategic goal, the net cost of operations for the reporting period. Net cost of operations consists of full program costs incurred by the SBA less the exchange revenues earned by those programs.

The **Consolidated Statement of Changes in Net Position** presents SBA's beginning and ending net position by two components – Cumulative Results of Operations and Unexpended Appropriations. It summarizes the change in net position by major transaction category. The ending balances of both components of net position are also reported on the Balance Sheet.

The **Combined Statement of Budgetary Resources** provides information about funding and availability of budgetary resources, and the status of those resources at the end of the reporting period. Data on the Combined Statement of Budgetary Resources is consistent with information reflected on the Report on Budget Execution and Budgetary Resources (SF 133), with the one exception of offsetting receipts. Offsetting receipts offset budget authority and outlays at the agency level in the Budget of the United States Government, but are not reflected in the SF 133. The SBA includes offsetting receipts in this statement for the purpose of reconciling outlay information presented in the Budget of the United States Government.

The **Notes to the Financial Statements** provide information to explain the basis of the accounting and presentation used to prepare the statements and to explain specific items in the statements. They also provide information to support how particular accounts have been valued and computed.

The **Required Supplementary Information** presents a Combining Statement of Budgetary Resources report by principal functional area.

The **Required Supplementary Stewardship Information** provides information on SBA's investment in human capital that supports the increase or maintenance of national economic productivity capacity through education and training programs.

U. S. Small Business Administration  
**Consolidated Balance Sheet**  
as of September 30, 2014 and 2013

(Dollars in Thousands)

|  | <b>2014</b>          | <b>2013</b>          |
|--|----------------------|----------------------|
| <b>ASSETS</b>  |                      |                      |
| Intragovernmental Assets   |                      |                      |
| Fund Balance with Treasury (Note 2)                                      | \$ 6,110,111         | \$ 6,198,604         |
| Advances (Note 1)  | 28,173               | 16,523               |
| <b>Total Intragovernmental Assets</b>                                    | <b>6,138,284</b>     | <b>6,215,127</b>     |
| Assets - Public and Other  |                      |                      |
| Cash (Note 3)  | 1,264                | 3,976                |
| Accounts Receivable, Net (Note 5)  | 83,816               | 84,097               |
| Credit Program Receivables and Related Foreclosed Property, Net (Note 6) | 6,946,903            | 7,534,448            |
| General Property and Equipment, Net (Note 7)                             | 4,729                | 6,173                |
| Advances (Note 1)  | 9,255                | 2,349                |
| <b>Total Assets - Public and Other</b>                                   | <b>7,045,967</b>     | <b>7,631,043</b>     |
| <b>Total Assets</b>  | <b>\$ 13,184,251</b> | <b>\$ 13,846,170</b> |
| <b>LIABILITIES</b>   |                      |                      |
| Intragovernmental Liabilities  |                      |                      |
| Interest Payable   | \$ 864               | \$ 832               |
| Debt (Note 9)  | 7,756,100            | 8,088,099            |
| Net Assets of Liquidating Funds Due to Treasury (Note 10)                | 10,140               | 41,698               |
| Downward Reestimate Payable to Treasury (Note 1, Note 13)                | 1,637,283            | 1,116,192            |
| Other (Note 8, Note 11)  | 9,984                | 9,652                |
| <b>Total Intragovernmental Liabilities</b>                               | <b>9,414,371</b>     | <b>9,256,473</b>     |
| Other Liabilities - Public   |                      |                      |
| Accounts Payable (Note 1)  | 47,707               | 45,972               |
| Accrued Grant Liability (Note 1)   | 77,000               | 73,000               |
| Liability for Loan Guaranties (Note 6)                                   | 2,044,509            | 2,987,263            |
| Federal Employees' Compensation Act Actuarial Liability (Note 1, Note 8) | 34,627               | 33,703               |
| Surety Bond Guarantee Program Future Claims (Note 8)                     | 35,799               | 31,029               |
| Other (Note 8, Note 11)  | 41,790               | 34,876               |
| <b>Total Other Liabilities - Public</b>                                  | <b>2,281,432</b>     | <b>3,205,843</b>     |
| <b>Total Liabilities</b>   | <b>11,695,803</b>    | <b>12,462,316</b>    |
| <b>NET POSITION</b>  |                      |                      |
| Unexpended Appropriations (Note 1)                                       | 1,692,804            | 1,753,736            |
| Cumulative Results of Operations (Note 1)                                | (204,356)            | (369,882)            |
| <b>Total Net Position</b>  | <b>1,488,448</b>     | <b>1,383,854</b>     |
| <b>Total Liabilities and Net Position</b>                                | <b>\$ 13,184,251</b> | <b>\$ 13,846,170</b> |

The accompanying notes are an integral part of these statements.

U. S. Small Business Administration  
**Consolidated Statement of Net Cost**  
 For the years ended September 30, 2014 and 2013

(Dollars in Thousands)

|  | <b>2014</b>         | <b>2013</b>       |
|--|---------------------|-------------------|
| <b>STRATEGIC GOAL 1:</b>   |                     |                   |
| <b>Growing Businesses and Creating Jobs</b>  |                     |                   |
| Gross Cost   | \$ (107,258)        | \$ 1,002,050      |
| Less: Earned Revenue   | 511,728             | 614,595           |
| <b>Net Cost of Strategic Goal 1</b>  | <b>(618,986)</b>    | <b>387,455</b>    |
| <b>STRATEGIC GOAL 2:</b>   |                     |                   |
| <b>Serving as the Voice for Small Business</b>   |                     |                   |
| Gross Cost   | 109,488             | 92,964            |
| <b>Total Program Cost of Strategic Goal 2</b>  | <b>109,488</b>      | <b>92,964</b>     |
| <b>STRATEGIC GOAL 3:</b>   |                     |                   |
| <b>Building an SBA that Meets the Needs of Today's and Tomorrow's Small Businesses</b> |                     |                   |
| Gross Cost   | 25,830              | 5,908             |
| <b>Total Program Cost of Strategic Goal 3</b>  | <b>25,830</b>       | <b>5,908</b>      |
| <b>COST NOT ASSIGNED TO STRATEGIC GOALS</b>  |                     |                   |
| Gross Cost   | 17,274              | 37,759            |
| <b>Total Program Cost Not Assigned to Strategic Goals</b>                              | <b>17,274</b>       | <b>37,759</b>     |
| <b>Net Cost of Operations</b>  | <b>\$ (466,394)</b> | <b>\$ 524,086</b> |

**Note 14**

The accompanying notes are an integral part of these statements.

DID  
YOU  
KNOW

For the first time in eight years, the federal government met the 23 percent small business contracting goal, purchasing **\$83 billion** in goods and services from small businesses through prime contracting procurements totaling 23.39 percent.

For more information visit:  
<http://www.sba.gov/content/small-business-procurement-scorecards-0>.

U. S. Small Business Administration  
**Consolidated Statement of Changes in Net Position**

For the years ended September 30, 2014 and 2013

(Dollars in Thousands)

|   | <b>2014</b>         | <b>2013</b>         |
|---|---------------------|---------------------|
| <b>Beginning Cumulative Results of Operations</b>   | <b>\$ (369,882)</b> | <b>\$ (907,005)</b> |
| <b>Budgetary Financing Sources</b>                  |                     |                     |
| Appropriations Used                                 | 1,325,564           | 2,169,146           |
| Donations of Cash and Cash Equivalents              | 40                  | 20                  |
| <b>Other Financing Sources</b>                      |                     |                     |
| Imputed Financing from Costs Absorbed by Others     | 21,893              | 19,955              |
| Other - Current Year Liquidating Equity Activity    | (3,218)             | (3,992)             |
| Other - Non-entity Activity                         | (1,645,147)         | (1,123,920)         |
| <b>Total Financing Sources</b>                      | <b>(300,868)</b>    | <b>1,061,209</b>    |
| <b>Less: Net Cost of Operations</b>                 | <b>(466,394)</b>    | <b>524,086</b>      |
| <b>Ending Cumulative Results of Operations</b>      | <b>\$ (204,356)</b> | <b>\$ (369,882)</b> |
| <b>Beginning Unexpended Appropriations</b>          | <b>\$ 1,753,736</b> | <b>\$ 1,281,279</b> |
| <b>Budgetary Financing Sources</b>                  |                     |                     |
| Appropriations Received                             | 1,278,241           | 2,745,037           |
| Rescissions   | -                   | (95,281)            |
| Adjustment - Cancelled Authority                    | (9,434)             | (5,194)             |
| Return of Unrequired Liquidating Fund Appropriation | (3,534)             | -                   |
| Other Adjustments                                   | (641)               | (2,959)             |
| Appropriations Used                                 | (1,325,564)         | (2,169,146)         |
| <b>Total Budgetary Financing Sources</b>            | <b>(60,932)</b>     | <b>472,457</b>      |
| <b>Ending Unexpended Appropriations</b>             | <b>\$ 1,692,804</b> | <b>\$ 1,753,736</b> |
| <b>Ending Net Position</b>                          | <b>\$ 1,488,448</b> | <b>\$ 1,383,854</b> |

The accompanying notes are an integral part of these statements.

U. S. Small Business Administration  
**Combined Statement of Budgetary Resources**

For the years ended September 30, 2014 and 2013

(Dollars in Thousands)

|   | <b>September 30, 2014</b> |                                   |                      |
|---|---------------------------|-----------------------------------|----------------------|
|   | <b>Budgetary</b>          | <b>Nonbudgetary<br/>Financing</b> | <b>Total</b>         |
| <b>BUDGETARY RESOURCES</b>  |                           |                                   |                      |
| Unobligated Balance Brought Forward, October 1  | \$ 1,297,199              | \$ 4,136,787                      | \$ 5,433,986         |
| Recoveries of Prior Year Obligations  | 105,039                   | 317,098                           | 422,137              |
| Other Changes in Unobligated Balance  | (34,053)                  | (965,794)                         | (999,847)            |
| Unobligated Balance from Prior Year Budget Authority, net                                     | 1,368,185                 | 3,488,091                         | 4,856,276            |
| Appropriations (discretionary and mandatory)  | 1,274,707                 | -                                 | 1,274,707            |
| Borrowing Authority (discretionary and mandatory)   | -                         | 762,945                           | 762,945              |
| Spending Authority from Offsetting Collections  | 381,357                   | 3,551,374                         | 3,932,731            |
| <b>Total Budgetary Resources</b>  | <b>\$ 3,024,249</b>       | <b>\$ 7,802,410</b>               | <b>\$ 10,826,659</b> |
| <b>STATUS OF BUDGETARY RESOURCES</b>  |                           |                                   |                      |
| Obligations Incurred  | \$ 1,661,198              | \$ 3,453,214                      | \$ 5,114,412         |
| Unobligated Balance, end of year:   |                           |                                   |                      |
| Apportioned   | 398,548                   | 1,586,238                         | 1,984,786            |
| Unapportioned   | 964,503                   | 2,762,958                         | 3,727,461            |
| Total Unobligated Balance, end of year  | 1,363,051                 | 4,349,196                         | 5,712,247            |
| <b>Total Status of Budgetary Resources</b>  | <b>\$ 3,024,249</b>       | <b>\$ 7,802,410</b>               | <b>\$ 10,826,659</b> |
| <b>CHANGE IN OBLIGATED BALANCE</b>  |                           |                                   |                      |
| <i>Unpaid Obligations:</i>  |                           |                                   |                      |
| Unpaid Obligations, Brought Forward, October 1  | \$ 639,951                | \$ 701,530                        | \$ 1,341,481         |
| Obligations Incurred  | 1,661,198                 | 3,453,214                         | 5,114,412            |
| Gross Outlays   | (1,710,912)               | (3,592,085)                       | (5,302,997)          |
| Recoveries of Prior Year Unpaid Obligations   | (105,039)                 | (317,098)                         | (422,137)            |
| Unpaid Obligations, end of year   | 485,198                   | 245,561                           | 730,759              |
| <i>Uncollected Payments:</i>  |                           |                                   |                      |
| Uncollected Payments, Federal Sources, brought forward, October 1                             | -                         | (296,519)                         | (296,519)            |
| Change in Uncollected Payments, Federal Sources   | -                         | 153,510                           | 153,510              |
| Uncollected Payments, Federal Sources, end of year  | -                         | (143,009)                         | (143,009)            |
| <i>Memorandum (non-add) entries:</i>  |                           |                                   |                      |
| <b>Obligated Balance, start of year</b>   | <b>\$ 639,951</b>         | <b>\$ 405,011</b>                 | <b>\$ 1,044,962</b>  |
| <b>Obligated Balance, end of year</b>   | <b>\$ 485,198</b>         | <b>\$ 102,552</b>                 | <b>\$ 587,750</b>    |
| <b>BUDGET AUTHORITY AND OUTLAYS, NET</b>  |                           |                                   |                      |
| Budget Authority, gross (discretionary and mandatory)   | \$ 1,656,064              | \$ 4,314,319                      | \$ 5,970,383         |
| Actual Offsetting Collections (discretionary and mandatory)                                   | (392,155)                 | (3,923,558)                       | (4,315,713)          |
| Change in Uncollected Customer Payments<br>from Federal Sources (discretionary and mandatory) | -                         | 153,510                           | 153,510              |
| <b>Budget Authority, net (discretionary and mandatory)</b>                                    | <b>\$ 1,263,909</b>       | <b>\$ 544,271</b>                 | <b>\$ 1,808,180</b>  |
| Gross Outlays (discretionary and mandatory)   | \$ 1,710,912              | \$ 3,592,085                      | \$ 5,302,997         |
| Actual Offsetting Collections (discretionary and mandatory)                                   | (392,155)                 | (3,923,558)                       | (4,315,713)          |
| Net Outlays (discretionary and mandatory)   | 1,318,757                 | (331,473)                         | 987,284              |
| Distributed Offsetting Receipts   | 900                       | (1,124,055)                       | (1,123,155)          |
| <b>Agency Outlays, net (discretionary and mandatory)</b>                                      | <b>\$ 1,319,657</b>       | <b>\$ (1,455,528)</b>             | <b>\$ (135,871)</b>  |

**Note 15**

The accompanying notes are an integral part of these statements.

U. S. Small Business Administration  
**Combined Statement of Budgetary Resources** (continued)

For the years ended September 30, 2014 and 2013

(Dollars in Thousands)

|   | <b>September 30, 2013</b> |                                   |                      |
|---|---------------------------|-----------------------------------|----------------------|
|   | <b>Budgetary</b>          | <b>Nonbudgetary<br/>Financing</b> | <b>Total</b>         |
| <b>BUDGETARY RESOURCES</b>  |                           |                                   |                      |
| Unobligated Balance Brought Forward, October 1  | \$ 862,901                | \$ 4,769,467                      | \$ 5,632,368         |
| Recoveries of Prior Year Obligations  | 63,684                    | 81,655                            | 145,339              |
| Other Changes in Unobligated Balance  | (22,648)                  | (595,820)                         | (618,468)            |
| Unobligated Balance from Prior Year Budget Authority, net                                     | 903,937                   | 4,255,302                         | 5,159,239            |
| Appropriations (discretionary and mandatory)  | 2,649,756                 | –                                 | 2,649,756            |
| Borrowing Authority (discretionary and mandatory)   | –                         | 1,520,370                         | 1,520,370            |
| Spending Authority from Offsetting Collections  | 625,835                   | 4,104,394                         | 4,730,229            |
| <b>Total Budgetary Resources</b>  | <b>\$ 4,179,528</b>       | <b>\$ 9,880,066</b>               | <b>\$ 14,059,594</b> |
| <b>STATUS OF BUDGETARY RESOURCES</b>  |                           |                                   |                      |
| Obligations Incurred  | \$ 2,882,329              | \$ 5,743,279                      | \$ 8,625,608         |
| Unobligated Balance, end of year:   |                           |                                   |                      |
| Apportioned   | 594,338                   | 854,066                           | 1,448,404            |
| Unapportioned   | 702,861                   | 3,282,721                         | 3,985,582            |
| Total Unobligated Balance, end of year  | 1,297,199                 | 4,136,787                         | 5,433,986            |
| <b>Total Status of Budgetary Resources</b>  | <b>\$ 4,179,528</b>       | <b>\$ 9,880,066</b>               | <b>\$ 14,059,594</b> |
| <b>CHANGE IN OBLIGATED BALANCE</b>  |                           |                                   |                      |
| <u>Unpaid Obligations:</u>  |                           |                                   |                      |
| Unpaid Obligations, Brought Forward, October 1  | \$ 619,996                | \$ 278,173                        | \$ 898,169           |
| Obligations Incurred  | 2,882,329                 | 5,743,279                         | 8,625,608            |
| Gross Outlays   | (2,798,690)               | (5,238,267)                       | (8,036,957)          |
| Recoveries of Prior Year Unpaid Obligations   | (63,684)                  | (81,655)                          | (145,339)            |
| Unpaid Obligations, end of year   | 639,951                   | 701,530                           | 1,341,481            |
| <u>Uncollected Payments:</u>  |                           |                                   |                      |
| Uncollected Payments, Federal Sources, brought forward, October 1                             | –                         | (176,681)                         | (176,681)            |
| Change in Uncollected Payments, Federal Sources   | –                         | (119,838)                         | (119,838)            |
| Uncollected Payments, Federal Sources, end of year  | –                         | (296,519)                         | (296,519)            |
| <u>Memorandum (non-add) entries:</u>  |                           |                                   |                      |
| <b>Obligated Balance, start of year</b>   | <b>\$ 619,996</b>         | <b>\$ 101,492</b>                 | <b>\$ 721,488</b>    |
| <b>Obligated Balance, end of year</b>   | <b>\$ 639,951</b>         | <b>\$ 405,011</b>                 | <b>\$ 1,044,962</b>  |
| <b>BUDGET AUTHORITY AND OUTLAYS, NET</b>  |                           |                                   |                      |
| Budget Authority, gross (discretionary and mandatory)   | \$ 3,275,591              | \$ 5,624,764                      | \$ 8,900,355         |
| Actual Offsetting Collections (discretionary and mandatory)                                   | (625,895)                 | (4,540,597)                       | (5,166,492)          |
| Change in Uncollected Customer Payments<br>from Federal Sources (discretionary and mandatory) | –                         | (119,838)                         | (119,838)            |
| <b>Budget Authority, net (discretionary and mandatory)</b>                                    | <b>\$ 2,649,696</b>       | <b>\$ 964,329</b>                 | <b>\$ 3,614,025</b>  |
| Gross Outlays (discretionary and mandatory)   | \$ 2,798,690              | \$ 5,238,267                      | \$ 8,036,957         |
| Actual Offsetting Collections (discretionary and mandatory)                                   | (625,895)                 | (4,540,597)                       | (5,166,492)          |
| Net Outlays (discretionary and mandatory)   | 2,172,795                 | 697,670                           | 2,870,465            |
| Distributed Offsetting Receipts   | (118)                     | (1,696,861)                       | (1,696,979)          |
| <b>Agency Outlays, net (discretionary and mandatory)</b>                                      | <b>\$ 2,172,677</b>       | <b>\$ (999,191)</b>               | <b>\$ 1,173,486</b>  |

**Note 15**

The accompanying notes are an integral part of these statements.

## NOTE 1 SIGNIFICANT ACCOUNTING POLICIES

### Reporting Entity

The Small Business Act of 1953 created the Small Business Administration as an independent federal agency. SBA's mission is to maintain and strengthen the nation's economy by enabling the establishment and vitality of small businesses and by assisting in the economic recovery of communities after disasters. The SBA operates through the execution of a congressionally approved budget that funds its programs.

### Basis of Accounting and Presentation

The SBA prepares financial statements to report its financial position and results of its operations as required by the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994. The financial statements are prepared from the Agency's records in accordance with generally accepted accounting principles using formats prescribed by the Office of Management and Budget. As a federal agency, the SBA cannot incur obligations without authority from the Congress and an apportionment by the OMB.

These financial statements reflect transactions recorded on both a proprietary accrual accounting basis and a budgetary obligation basis, in accordance with concepts and guidance provided by the OMB, the Federal Accounting Standards Advisory Board, and the Department of the Treasury. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to receipt or payment of cash. Budgetary accounting recognizes the legal commitment or obligation of funds in advance of the proprietary accruals and facilitates compliance with legal constraints and controls over the use of federal funds.

The Federal Credit Reform Act of 1990 governs SBA's accounting for direct loans and loan guaranties made in FY 1992 and thereafter. Under the FCRA, the liability for loan guaranties is determined as the summarized discounted present value of the estimated future net cash inflows and outflows for each fiscal year's cohort of guaranties. For direct loans, the allowance is the current outstanding FCRA loans receivable balance less the discounted present value of the estimated future net cash flows for all the loan cohorts. A cohort of loans receivable or guarantied loans is all of the loans made in a given fiscal year. Increases to individual loans in a cohort that are made in a subsequent fiscal year are accounted for in the subsequent year's loan cohort. Cohort cash flows include loan repayments, recoveries on defaulted guaranties, and loan fees received by the SBA that are due from the lenders and borrowers when the loan is made and during the life of the loan cohort, as well as expenditures by the SBA for defaulted guaranties, loan servicing expenses, and other required SBA expenditures. An initial allowance or liability for loan guaranties is established in the original year of the loan cohort. The initial amount of the allowance and liability for each cohort is reestimated annually at fiscal year-end, and the adjusted amount is included in SBA's annual financial statements. Note 6 further describes FCRA accounting.

### Use of Estimates

SBA's management makes assumptions and uses estimates to prepare the financial statements based upon the facts that exist when the statements are prepared. The SBA also uses economic assumptions provided by the Office of Management and Budget in preparing the estimates. Actual results may differ from those assumptions and estimates and the differences may be significant. The most significant differences between actual results and these estimates may occur in the valuation of credit program receivables and liabilities for loan guaranties under guidelines in the Federal Credit Reform Act of 1990. The SBA recognizes the sensitivity of credit reform modeling to slight changes in some model assumptions and therefore continually reviews its model factors and statistical modeling techniques to reflect the most accurate credit program costs possible in its annual financial statements.

## Budgets and Budgetary Accounting for Loan Programs

SBA's loan disbursements are financed by appropriations for long-term loan subsidy cost and borrowings from the Treasury's Bureau of the Fiscal Service for the remaining non-subsidized portion of the loans. The Congress may provide one year, multi-year, or no year appropriations to cover the estimated long-term costs of the loan programs. The non-subsidized portion of each loan disbursement, financed initially under permanent indefinite authority to borrow funds from the Treasury, is repaid from collections of loan fees, repayments, and default recoveries. The Congress authorizes the dollar amount of obligations that can be made for the cost of direct loans and loan guaranties and establishes the maximum amount of loans the SBA can guarantee in its annual appropriation bill.

A permanent indefinite authority is available to fund any reestimated increase of subsidy costs that occurs after the year in which a loan is disbursed. Reestimated reductions of subsidy costs are returned to the Treasury and are unavailable to the SBA. As required by the Federal Credit Reform Act of 1990, the SBA uses budgetary "program accounts" to account for appropriations in its credit programs and nonbudgetary "financing accounts" to account for credit program cash flow. Estimates and reestimates of credit program subsidy expenses are recorded in SBA's program accounts. Financing accounts are used to account for Treasury borrowings, the collection of loan fees, repayments and default recoveries, and the disbursement of loans and loan expenses.

## Accounts Payable

Accounts Payable are amounts due to public entities that will be liquidated during the next operating cycle. Included in the liability are payables to SBA lenders for their share of loan collections and to vendors for goods and services.

## Accrued Grant Liability

Disbursements of grant funds are recognized as expenses at the time of disbursement. However, some grant recipients incur expenditures prior to initiating a request for disbursement based on the nature of the expenditures. The SBA accrues a liability for expenditures incurred by grantees prior to receiving grant funds for the expenditures. The amount to be accrued is determined through an analysis of historic grant expenditures. The Small Business Development Center program and several other grant programs are subject to this treatment.

## Advances

The SBA has both intragovernmental advances and advances to the public. Intragovernmental advances are to the Interior Business Center of the Department of the Interior, for contracting assistance on work not yet performed. Advances to the public represent prepaid grants to counseling and training partners.

## Contingencies

The SBA is a party in various administrative proceedings, legal actions, environmental suits and claims brought against the Agency. In the opinion of SBA's management and legal counsel, the ultimate resolution of these proceedings, actions, suits, and claims will not materially affect the financial position or results of SBA's operations.

## Cumulative Results of Operations

The deficit in Cumulative Results of Operations, presented on the Balance Sheet and on the Statement of Changes in Net Position, is the accumulated difference between expenses and financing sources since the inception of the Agency. The deficits reported reflect timing differences between the recording of expenses and the recognition of resources. Most of this timing difference results from subsidy reestimates which are funded in the following year.

## Unexpended Appropriations

Unexpended Appropriations is the portion of SBA's appropriations received which are either undelivered or unobligated. Delivered orders result in expended appropriations and reduce the total reported as Unexpended Appropriations. Undelivered orders are the amount of orders of goods or services which have not been actually or constructively received.

## Reclassifications

As discussed in Note 14, certain FY 2013 financial statement line items have been reclassified to conform with the current year presentation. The reclassifications had no material effect on total assets, liabilities, net position, or net cost of operations as previously reported.

## Employee Benefits

### Leave

A liability for employee annual leave is accrued as it is earned and reduced as leave is taken. Each year the balance of accrued annual leave is adjusted to reflect current pay rates as well as forfeited "use or lose" leave. Amounts are reported as unfunded to the extent current or prior year appropriations are not available to fund annual leave earned but not taken. Sick leave and other types of non-vested leave are expensed as taken.

### Employee Health and Life Insurance Benefits

SBA employees may choose to participate in the contributory Federal Employees Health Benefits and the Federal Employees Group Life Insurance programs. The SBA matches a portion of the employee contributions to each program. Such matching contributions are recognized as current operating expenses.

### Employee Pension Benefits

SBA employees participate in either the Civil Service Retirement System or the Federal Employees Retirement System and Social Security. These systems provide benefits upon retirement and in the event of death, disability or other termination of employment and may also provide pre-retirement benefits. They may also include benefits to survivors and their dependents, and they may contain early retirement or other special features. SBA's contributions to both retirement plans, as well as to the government-wide Federal Insurance Contribution Act, administered by the Social Security Administration, are recognized on the Consolidated Statement of Net Cost as current operating expenses.

Federal employee benefits also include the Thrift Savings Plan. For FERS employees the SBA matches employee contributions to the plan, subject to limitations. The matching contributions are recognized as current operating expenses.

### Imputed Financing Costs

The SBA recognizes the full cost of providing all employee benefits and future retirement benefits, including life and health insurance, at the time employee services are rendered. Eligible retired SBA employees can continue to participate in health and life insurance plans. The cost of these benefits is funded through Agency contributions, employee compensation to the extent withheld from employee and retiree pay, from matching of employee withholding for Thrift Savings Plan and FICA, and by the Office of Personnel Management which administers the retirement programs for SBA employees.

The OPM calculates imputed costs as the actuarial present value of future benefits attributed to services rendered by covered employees and eligible retired SBA employees during the accounting period, net of the amounts contributed by employees, retirees, and the Agency. The SBA recognizes these imputed costs in the Statement of Net Cost and imputed financing in determining SBA's net position.

### Federal Employees' Compensation Act

The Federal Employees' Compensation Act provides income and medical cost protection to covered federal civilian employees injured on the job and to beneficiaries of employees whose deaths are attributable to job-related injury

or disease. The FECA program is administered by the Department of Labor. Labor pays valid claims as they occur, which are billed to the SBA annually and funded and paid approximately 15 months later. Labor also calculates an estimated actuarial liability for future benefits based upon historical experience and other economic variables. Projected annual benefit payments are then discounted to present value using the forecasted interest rates for 10-year Treasury notes and bonds published by the OMB in its economic assumptions for the federal budget. The SBA recognizes a current unfunded cost for the actual claims paid and the change in the FECA actuarial liability each year.

## NOTE 2 FUND BALANCE WITH TREASURY

The Department of the Treasury processes cash receipts and disbursements on SBA's behalf to pay liabilities and finance loan program costs. Cash receipts are deposited into SBA's account at the Treasury. SBA's fund balances with the Treasury are available to make expenditures to liquidate allowable obligations, except for the Non-entity Fund Balance which is not available to the SBA to obligate or expend. Separate records are maintained for SBA's program, financing, liquidating, suspense/budget clearing accounts and other accounts. Fund balances at the Treasury include expired year amounts, which are unavailable for obligation, as well as amounts currently available for new obligations.

(Dollars in Thousands)

| As of September 30,                            | 2014                | 2013                |
|--|---------------------|---------------------|
| Appropriated Funds                             | \$ 1,766,183        | \$ 1,835,332        |
| Financing Funds                                | 4,260,921           | 4,261,451           |
| Liquidating Funds                              | 1,124               | 28,338              |
| Revolving Fund                                 | 80,779              | 73,343              |
| Trust Fund                                     | 162                 | 136                 |
| <b>Total Entity Fund Balance with Treasury</b> | <b>6,109,169</b>    | <b>6,198,600</b>    |
| Non-entity Fund Balance                        | –                   | 4                   |
| Budget Clearing Account Balance                | 942                 | –                   |
| <b>Total Fund Balance with Treasury</b>        | <b>\$ 6,110,111</b> | <b>\$ 6,198,604</b> |
| <b>Status of Fund Balance with Treasury</b>    |                     |                     |
| Unobligated Balance Available                  | \$ 1,984,786        | \$ 1,448,404        |
| Unobligated Balance Unavailable                | 3,727,461           | 3,985,582           |
| Obligated Balance Not Yet Disbursed            | 587,750             | 1,044,962           |
| Borrowing Authority Not Converted to Funds     | (190,828)           | (280,348)           |
| Nonbudgetary                                   | 942                 | 4                   |
| <b>Total Fund Balance with Treasury</b>        | <b>\$ 6,110,111</b> | <b>\$ 6,198,604</b> |

Unobligated balances become available when OMB approves SBA's request to apportion funds for obligation in the current fiscal year. Obligated balances not yet disbursed include unpaid obligations offset by uncollected customer payments from other federal government accounts. The unobligated and obligated balances are reflected on the Statement of Budgetary Resources.

## NOTE 3 CASH

The SBA field offices deposit collections from borrowers in SBA's account at the Treasury using an electronic deposit system. At the end of the fiscal year, collections temporarily held by SBA field offices pending deposit are recorded as Undeposited Collections – Cash in Transit and totaled \$1.3 million and \$3.9 million at September 30, 2014 and 2013.

## NOTE 4 FIDUCIARY ACTIVITIES: MASTER RESERVE FUND AND MASTER RESERVE ACCOUNT

Fiduciary activities are the receipt, management, protection, accounting, investment and disposition by the federal government of cash or other assets in which non-federal entities have an ownership interest that the federal government must uphold. Fiduciary cash and other assets are not assets of the government, and are not recognized on SBA's proprietary statements, but they are required to be disclosed in the notes to SBA's financial statements. SBA's fiduciary balances are on deposit in commercial banks.

The Master Reserve Fund is a fiduciary activity administered by SBA's fiscal agent, Colson Services Corp., a subsidiary of the Bank of New York Mellon. The balance in the MRF is invested according to SBA policy entirely in Treasury securities and repurchase agreements that are backed by Treasury securities. The MRF is an integral part of SBA's 7(a) secondary market program. The MRF was authorized by the Small Business Secondary Market Improvement Act of 1984 to facilitate the pooling of 7(a) guaranteed loans that are purchased by secondary market investors. The 7(a) secondary market program includes SBA's guaranty of timely payment, as well as a default guaranty, to 7(a) secondary market investors. The MRF supports \$22.5 billion and \$20.5 billion of outstanding SBA guaranteed 7(a) loan principal in the secondary market at September 30, 2014 and 2013.

The Master Reserve Account is an SBA fiduciary activity that is administered for the SBA by Wells Fargo. The balance in the MRA is invested entirely in Treasury securities. The MRA facilitates the operation of the 504 Certified Development Company secondary market program. The MRA was authorized by Section 505 of the Small Business Investment Act of 1958 as amended, as a vehicle to receive, temporarily hold, and distribute 504 program cash flows. The MRA receives monthly payments from the 504 borrowers, and retains the payments until a semi-annual debenture payment is due to the secondary market investors. The 504 secondary market program includes SBA's guaranty of timely payment, as well as a default guaranty, to 504 secondary market investors. The MRA supports \$28.4 billion and \$28.1 billion of SBA guaranteed 504 debentures outstanding in the secondary market at September 30, 2014 and 2013.

The composition of the MRF and MRA and a reconciliation of the changes in the assets are included in the following table.

### Master Reserve Fund and Master Reserve Account

(Dollars in Thousands)

#### FIDUCIARY ASSETS

| As of September 30,                         | 2014                |                   |                     | 2013                |                   |                     |
|---|---------------------|-------------------|---------------------|---------------------|-------------------|---------------------|
|   | MRF                 | MRA               | Total               | MRF                 | MRA               | Total               |
| <b>Cash</b>                                 | \$ 44,994           | \$ -              | \$ 44,994           | \$ -                | \$ -              | \$ -                |
| <b>Short Term Securities</b>                |                     |                   |                     |                     |                   |                     |
| Money Market Funds                          | 76,758              | 636,789           | 713,547             | 13,659              | 700,760           | 714,419             |
| Treasury Bills                              | 404,924             | -                 | 404,924             | -                   | -                 | -                   |
| Repurchase Agreements                       | 223,892             | -                 | 223,892             | 567,511             | -                 | 567,511             |
| <b>Total Cash and Short Term Securities</b> | <b>750,568</b>      | <b>636,789</b>    | <b>1,387,357</b>    | <b>581,170</b>      | <b>700,760</b>    | <b>1,281,930</b>    |
| <b>Long Term Securities</b>                 |                     |                   |                     |                     |                   |                     |
| Treasury Notes Including Interest           | 2,113,153           | -                 | 2,113,153           | 2,087,658           | -                 | 2,087,658           |
| <b>Total Long Term Securities</b>           | <b>2,113,153</b>    | <b>-</b>          | <b>2,113,153</b>    | <b>2,087,658</b>    | <b>-</b>          | <b>2,087,658</b>    |
| <b>Net Assets</b>                           | <b>\$ 2,863,721</b> | <b>\$ 636,789</b> | <b>\$ 3,500,510</b> | <b>\$ 2,668,828</b> | <b>\$ 700,760</b> | <b>\$ 3,369,588</b> |

## Master Reserve Fund and Master Reserve Account

*(Dollars in Thousands)*

## RECONCILIATION OF FIDUCIARY ASSETS

| For the Years Ending September 30, | 2014                |                   |                     | 2013                |                   |                     |
|------------------------------------|---------------------|-------------------|---------------------|---------------------|-------------------|---------------------|
|                                    | MRF                 | MRA               | Total               | MRF                 | MRA               | Total               |
| <b>Beginning Net Assets</b>        | \$ 2,668,828        | \$ 700,760        | \$ 3,369,588        | \$ 2,464,331        | \$ 518,214        | \$ 2,982,545        |
| <b>Receipts</b>                    |                     |                   |                     |                     |                   |                     |
| Earned Income                      | 33,616              | 106               | 33,722              | 41,352              | 608               | 41,960              |
| Contributions                      | 4,011,870           | 13,483,031        | 17,494,901          | 3,574,020           | 7,950,189         | 11,524,209          |
| Net Realized Gain (Loss)           | (4,239)             | –                 | (4,239)             | (1,366)             | –                 | (1,366)             |
| <b>Total Receipts</b>              | <b>4,041,247</b>    | <b>13,483,137</b> | <b>17,524,384</b>   | <b>3,614,006</b>    | <b>7,950,797</b>  | <b>11,564,803</b>   |
| <b>Less Disbursements</b>          |                     |                   |                     |                     |                   |                     |
| Payments to Investors              | 3,846,354           | 13,547,108        | 17,393,462          | 3,409,509           | 7,768,251         | 11,177,760          |
| <b>Total Disbursements</b>         | <b>3,846,354</b>    | <b>13,547,108</b> | <b>17,393,462</b>   | <b>3,409,509</b>    | <b>7,768,251</b>  | <b>11,177,760</b>   |
| <b>Ending Net Assets</b>           | <b>\$ 2,863,721</b> | <b>\$ 636,789</b> | <b>\$ 3,500,510</b> | <b>\$ 2,668,828</b> | <b>\$ 700,760</b> | <b>\$ 3,369,588</b> |

## NOTE 5 ACCOUNTS RECEIVABLE

Accounts receivable include amounts owed by the public for guaranty fees in SBA's loan and surety bond programs, refunds due from employees and others, as well as other amounts owed by lenders on guaranteed loans purchased by the SBA. An Allowance for Loss on uncollectible Surety Bond Guaranty fees is based on an aging of delinquent balances. The uncollectible amount for refunds and loan guaranty fees is not significant and no allowance is provided. Amounts over 180 days past due on guaranteed loans purchased by the SBA are written off for financial reporting purposes.

*(Dollars in Thousands)*

| As of September 30,      | 2014             | 2013             |
|--------------------------|------------------|------------------|
| <b>Public</b>            |                  |                  |
| Guaranty Fees Receivable | \$ 77,510        | \$ 78,355        |
| Refunds                  | 437              | 77               |
| Other                    | 5,899            | 5,670            |
| <b>Total Public</b>      | <b>83,846</b>    | <b>84,102</b>    |
| Allowance For Loss       | (30)             | (5)              |
| <b>Net Public</b>        | <b>\$ 83,816</b> | <b>\$ 84,097</b> |

## NOTE 6 CREDIT PROGRAM RECEIVABLES AND LIABILITY FOR LOAN GUARANTIES

### A. Loan Program Descriptions and Cost Determinations

#### Loan Program Descriptions

The SBA provides guaranties that help small businesses obtain bank loans and licensed companies to make investments in qualifying small businesses. The SBA also makes loans to microloan intermediaries and provides a direct loan program that assists homeowners, renters, and businesses to recover from disasters.

#### Major Direct Loan and Loan Guaranty Programs

| Program group | Program type | Program                                      |
|---------------|--------------|--|
| Disaster      | Direct       | Disaster Assistance Loans                    |
| Business      | Guarantied   | 7(a) Loan Guaranty                           |
| Business      | Guarantied   | 504 Certified Development Company            |
| Business      | Guarantied   | Small Business Investment Company Debentures |
| Business      | Direct       | 7(m) Microloan                               |

SBA's Disaster Assistance loan program makes direct loans to disaster victims under four categories: (1) loans for homes and personal property; (2) physical disaster loans to businesses of any size; (3) economic injury loans to small businesses without credit available elsewhere; and (4) economic injury loans to eligible businesses affected by essential employees called up to active duty in the military reserves. The maximum interest rate is 4 percent for loan applicants without credit available elsewhere and 8 percent for applicants with credit available elsewhere.

SBA's business loan programs include its flagship 7(a) Loan Guaranty program in which the SBA guarantees up to 90 percent of the principal amount of loans made by banks and other lending institutions to small businesses not able to obtain credit elsewhere.

The Section 504 Certified Development Company program guarantees 100 percent of the principal and interest payments on debentures issued by development companies that make small business loans secured primarily by real estate.

The Small Business Investment Company Debentures program guarantees principal and interest payments on securities issued by investment capital firms, which in turn make investments in small businesses.

The 7(m) Microloan program provides direct loans to nonprofit intermediaries, which use these funds to make loans up to \$50,000 to eligible small businesses.

#### Credit Program Receivables and Liability for Loan Guaranties

The Federal Credit Reform Act of 1990 governs direct loans made after FY 1991. FCRA loans are valued at the present value of expected future cash flows, discounted at the interest rate of marketable Treasury securities. The subsidy allowance represents the difference between the outstanding loans receivable balance and the net present value of the estimated cash flows of the loans over their remaining term. The subsidy allowance is subtracted from the outstanding loans receivable balance to obtain the net loans receivable balance. FCRA also governs loan guaranties made after FY 1991. A liability for outstanding guaranties is included on SBA's Balance Sheet. The liability is determined by calculating the net present value of expected future cash flows for outstanding guaranties in a manner similar to that used to determine the subsidy allowance for direct loans. Guarantied loans purchased by the SBA upon borrower default are established as loans receivable and are valued in a similar manner as direct loans under FCRA.

Direct loans made prior to FCRA are recorded at cost with an allowance for uncollectible amounts calculated using historical loss experience. For loan guaranties made prior to FCRA, a liability for expected future losses on outstanding guaranties is established based on historical experience. Guarantied loans purchased upon borrower default are established as loan receivables with an allowance for losses based on historical loss experience.

The SBA advances payments semiannually to honor its timely payment requirement of principal and interest due for debentures in SBA's Section 504 Certified Development Company and Small Business Investment Company programs. The advances are liquidated by receipt of the payments due from borrowers in these programs. To the extent that borrower payments may not repay advances, balances that remain collectible are reported as credit program receivables.

### Subsidy Funding under Federal Credit Reform

FCRA requires that the credit subsidy costs of direct loans and loan guaranties be expensed in the year loans are disbursed. The credit subsidy cost is the net present value of expected cash inflows and outflows over the life of a guarantied loan, or the difference between the net present value of expected cash flows and the face value of a direct loan. The cost expressed as a percentage of loans disbursed is termed the subsidy rate. The SBA receives appropriations annually to fund its credit programs based on the subsidy rate that applies to the credit program level approved by Congress. The SBA records subsidy expenses when loans are disbursed. In accordance with FCRA, subsidy costs are reestimated annually.

### Interest Receivable

Interest receivable is comprised of accrued interest on loans receivable and purchased interest related to defaulted guarantied loans. Interest income is accrued at the contractual rate on the outstanding principal amount and is reduced by the amount of interest income accrued on non-performing loans in excess of 90 days delinquent. Purchased interest is carried at cost. A 100 percent loss allowance is established for all purchased interest on non-performing loans.

### Foreclosed Property

Foreclosed property is comprised of real and business-related and personal property acquired through foreclosure on direct loans and defaulted loan guaranties. Properties acquired as a result of defaulted loans committed after FY 1991 are shown at recoverable value which is adjusted to the present value of expected future cash flows for financial statement presentation through the allowance for subsidy. Other foreclosed property is shown at the appraised value. At September 30, 2014 SBA's foreclosed property was \$43.0 million related to 93 loans. The properties had been held for an average of 860 days. At September 30, 2013 foreclosed property was \$47.3 million related to 84 loans. The properties had been held for an average of 868 days.

### Valuation Methodology for Post-1991 Direct Loans and Loan Guaranties

The value of direct and guarantied loans committed after FY 1991 is based on the net present value of their expected future cash flows. The SBA estimates future cash flows for guarantied and direct loans using economic and financial credit subsidy models. The SBA has developed a customized credit subsidy model for each of its major loan guaranty and direct loan programs.

SBA's models vary in the specific methodologies employed to forecast future program cash flows. In general, however, models for all major credit programs use historical data as the basis for assumptions about future program performance and then translate these assumptions into nominal cash flow estimates by applying rules about program structure. Nominal cash flow forecasts are discounted using the Office of Management and Budget's Credit Subsidy Calculator that has both forecasted and actual Treasury interest rates.

Historical data is used as the basis for program performance assumptions. The historical data undergoes quality review and analysis prior to its use in developing model assumptions.

Key input to the subsidy models varies by program. Input includes items such as:

- Contractual terms of the loan or guaranty such as loan amount, interest rate, maturity and grace period

- Borrower characteristics
- Loan origination methods
- Economic indicators such as gross domestic product growth and unemployment rate
- Loan performance assumptions, for example: conditional purchase and prepayment rates and recovery rates
- Loan fee rates

### Valuation Methodology for Pre-1992 Direct Loans and Loan Guaranties

The SBA values pre-credit reform direct and defaulted guaranteed loans by estimating an allowance for loan losses. This allowance is offset against gross loan receivables to obtain SBA's expected net collections from these assets. The SBA establishes a 100 percent allowance for pre-credit reform direct and guaranteed loans that are past due more than 180 days. A liability is also established for active pre-credit reform loan guaranties. The liability is estimated based on historical experience.

#### SUCCESS STORY: Babies' Comfort is Smart Business

Baby Elephant Ears Inc., Cambridge, Minnesota

**Alicia Overby**, SBA's *2014 Exporter of the Year*, is the founder and creator of Baby Elephant Ears, a small firm specializing in manufacturing, marketing, and exporting supportive pillows and other comfort accessories for babies. Out of sheer necessity, Alicia first had the idea for the product in 2008. In nine months, Baby Elephant Ears was launched. In five years, the company was selling its products at more than 850 locations in the U.S. and over a dozen countries.



Transitioning from home-based to thriving international business was not easy, but Alicia's commitment and hard work, coupled with SBDC assistance and two SBA loans, paid handsomely. Baby Elephant Ears also benefitted from the SBA STEP pilot program, which offers grants to states to promote export activities.

Alicia is heavily involved in sharing with other businesses and the community at large. Baby Elephant Ears "pays it forward" by mentoring other small business owners. The company also donates products to local charities and donated 500 pieces to a local missions trip to Guatemala. From a business that was originally financed with a loan against her husband's 401K, Baby Elephant Ears boasts sales of more than \$1.3 million annually.

## B. Credit Program Receivables and Related Foreclosed Property, Net

(Dollars in Thousands)

| <b>As of September 30, 2014</b>  | <b>Pre-1992 Loans</b> | <b>Post-1991 Loans</b> | <b>Total</b>        |
|--|-----------------------|------------------------|---------------------|
| <b>Direct Business Loans</b>   |                       |                        |                     |
| Business Loans Receivable  | \$ 5,727              | \$ 166,658             | \$ 172,385          |
| Interest Receivable  | 2,142                 | 683                    | 2,825               |
| Foreclosed Property  | 3,109                 | –                      | 3,109               |
| Allowance  | (8,268)               | (10,253)               | (18,521)            |
| <b>Total Direct Business Loans</b>   | <b>2,710</b>          | <b>157,088</b>         | <b>159,798</b>      |
| <b>Direct Disaster Loans</b>   |                       |                        |                     |
| Disaster Loans Receivable  | 3,707                 | 6,761,361              | 6,765,068           |
| Interest Receivable  | 140                   | 33,462                 | 33,602              |
| Foreclosed Property  | –                     | 2,409                  | 2,409               |
| Allowance  | (548)                 | (1,230,152)            | (1,230,700)         |
| <b>Total Direct Disaster Loans</b>   | <b>3,299</b>          | <b>5,567,080</b>       | <b>5,570,379</b>    |
| <b>Defaulted Guaranteed Business Loans &amp; Other Loans Receivable</b>        |                       |                        |                     |
| Defaulted Guaranteed Business Loans  | 8,436                 | 6,984,380              | 6,992,816           |
| Other Loans Receivable (see note below)  | –                     | 284,795                | 284,795             |
| Interest Receivable  | 656                   | 73,688                 | 74,344              |
| Foreclosed Property  | 2,070                 | 35,381                 | 37,451              |
| Allowance  | (8,407)               | (6,164,273)            | (6,172,680)         |
| <b>Total Defaulted Guaranteed Business Loans &amp; Other Loans Receivable</b>  | <b>2,755</b>          | <b>1,213,971</b>       | <b>1,216,726</b>    |
| <b>Total Credit Program Receivables &amp; Related Foreclosed Property, Net</b> |                       |                        | <b>\$ 6,946,903</b> |
| <b>As of September 30, 2013</b>  |                       |                        |                     |
|  | <b>Pre-1992 Loans</b> | <b>Post-1991 Loans</b> | <b>Total</b>        |
| <b>Direct Business Loans</b>   |                       |                        |                     |
| Business Loans Receivable  | \$ 8,958              | \$ 162,725             | \$ 171,683          |
| Interest Receivable  | 2,040                 | 757                    | 2,797               |
| Foreclosed Property  | 3,108                 | –                      | 3,108               |
| Allowance  | (7,036)               | (17,831)               | (24,867)            |
| <b>Total Direct Business Loans</b>   | <b>7,070</b>          | <b>145,651</b>         | <b>152,721</b>      |
| <b>Direct Disaster Loans</b>   |                       |                        |                     |
| Disaster Loans Receivable  | 5,226                 | 7,171,812              | 7,177,038           |
| Interest Receivable  | 223                   | 34,581                 | 34,804              |
| Foreclosed Property  | –                     | 1,690                  | 1,690               |
| Allowance  | (852)                 | (1,345,560)            | (1,346,412)         |
| <b>Total Direct Disaster Loans</b>   | <b>4,597</b>          | <b>5,862,523</b>       | <b>5,867,120</b>    |
| <b>Defaulted Guaranteed Business Loans &amp; Other Loans Receivable</b>        |                       |                        |                     |
| Defaulted Guaranteed Business Loans  | 9,264                 | 7,674,923              | 7,684,187           |
| Other Loans Receivable (see note below)  | –                     | 326,765                | 326,765             |
| Interest Receivable  | 580                   | 115,425                | 116,005             |
| Foreclosed Property  | 2,012                 | 40,501                 | 42,513              |
| Allowance  | (10,555)              | (6,644,308)            | (6,654,863)         |
| <b>Total Defaulted Guaranteed Business Loans &amp; Other Loans Receivable</b>  | <b>1,301</b>          | <b>1,513,306</b>       | <b>1,514,607</b>    |
| <b>Total Credit Program Receivables &amp; Related Foreclosed Property, Net</b> |                       |                        | <b>\$ 7,534,448</b> |

Note: Other Loans Receivable includes payments advanced by the SBA against future reimbursements in the SBIC and 504 Guaranty programs.

## C. Loans Disbursed and Outstanding Loan Obligations

(Dollars in Thousands)

### DIRECT LOANS

| <b>New Loans Disbursed During the Year Ending September 30,</b> | <b>2014</b>       | <b>2013</b>       |
|---|-------------------|-------------------|
| Business Direct Loan Program                                    | \$ 36,410         | \$ 42,305         |
| Disaster Loan Program   | 438,375           | 813,711           |
| <b>Total Direct Loans Disbursed</b>                             | <b>\$ 474,785</b> | <b>\$ 856,016</b> |
| <b>Outstanding Loan Obligations as of September 30,</b>         | <b>2014</b>       | <b>2013</b>       |
| Business Direct Loan Program                                    | \$ 40,669         | \$ 54,568         |
| Disaster Loan Program   | 156,158           | 605,591           |
| <b>Total Direct Loan Obligations</b>                            | <b>\$ 196,827</b> | <b>\$ 660,159</b> |

### GUARANTIED LOANS

| <b>New Loans Disbursed During the Year Ending September 30,</b> | <b>2014</b>   | <b>2013</b>   |
|---|---------------|---------------|
| Total Principal Disbursed at Face Value                         | \$ 22,453,725 | \$ 21,660,417 |
| Total Principal Disbursed Guaranteed by the SBA                 | 18,001,119    | 17,703,965    |
| <b>Outstanding Loan Obligations as of September 30,</b>         | <b>2014</b>   | <b>2013</b>   |
| Business Guaranteed Loan Programs                               | \$ 14,548,472 | \$ 14,370,509 |
| <b>Loans Outstanding as of September 30,</b>                    | <b>2014</b>   | <b>2013</b>   |
| Total Principal Outstanding at Face Value                       | \$ 99,013,624 | \$ 93,107,751 |
| Total Principal Outstanding Guaranteed by the SBA               | 83,505,973    | 79,064,486    |

SBA's guaranteed loan servicing agent provides data to the SBA on the unpaid principal balance of guaranteed loans within a precision of less than 1 percent due to timing.

## D. Subsidy Cost Allowance Balances

(Dollars in Thousands)

| <b>For the Years Ending September 30,</b>                       | <b>2014</b>         | <b>2013</b>         |
|---|---------------------|---------------------|
| <b>Post-1991 Business Direct and Purchased Guaranteed Loans</b> |                     |                     |
| <b>Beginning Balance of Allowance Account</b>                   | <b>\$ 6,662,139</b> | <b>\$ 6,974,670</b> |
| Current Year's Subsidy (see 6G for breakdown by component)      | 6,557               | 8,310               |
| Loans Written Off   | (1,446,655)         | (2,001,738)         |
| Subsidy Amortization  | (2,343)             | (1,446)             |
| Allowance Related to Guaranteed Loans Purchased This Year       | 820,625             | 1,538,325           |
| Miscellaneous Recoveries and Costs                              | 140,817             | 167,295             |
| Balance of Subsidy Allowance Account before Reestimates         | 6,181,140           | 6,685,416           |
| Technical Assumptions/Default Reestimates                       | (6,614)             | (23,277)            |
| <b>Ending Balance of Allowance Account</b>                      | <b>\$ 6,174,526</b> | <b>\$ 6,662,139</b> |
| <b>Post-1991 Disaster Direct Loans</b>                          |                     |                     |
| <b>Beginning Balance of Allowance Account</b>                   | <b>\$ 1,345,560</b> | <b>\$ 1,403,968</b> |
| Current Year's Subsidy (see 6G for breakdown by component)      | 44,394              | 90,673              |
| Loans Written Off   | (208,657)           | (179,963)           |
| Subsidy Amortization  | (12,096)            | (20,364)            |
| Miscellaneous Recoveries and Costs                              | 54,388              | 53,314              |
| Balance of Subsidy Allowance Account before Reestimates         | 1,223,589           | 1,347,628           |
| Technical Assumptions/Default Reestimates                       | 6,563               | (2,068)             |
| <b>Ending Balance of Allowance Account</b>                      | <b>\$ 1,230,152</b> | <b>\$ 1,345,560</b> |

## E. Liability for Loan Guaranties

(Dollars in Thousands)

| For the Years Ending September 30,                           | 2014                | 2013                |
|--|---------------------|---------------------|
| <b>Pre-1992 Business Loan Guaranties</b>                     |                     |                     |
| <b>Beginning Balance of Liability for Loan Guaranties</b>    | <b>\$ 45</b>        | <b>\$ 109</b>       |
| Adjustment to Expected Losses, Guaranties Outstanding        | 25                  | (64)                |
| <b>Ending Balance of Liability for Loan Guaranties</b>       | <b>70</b>           | <b>45</b>           |
| <b>Post-1991 Business Loan Guaranties</b>                    |                     |                     |
| <b>Beginning Balance of Liability for Loan Guaranties</b>    | <b>2,987,218</b>    | <b>3,725,842</b>    |
| Current Year's Subsidy (see 6G for breakdown by component)   | 143,867             | 275,742             |
| Fees   | 1,099,290           | 1,055,469           |
| Interest Accumulation Factor                                 | 108,690             | 186,436             |
| Claim Payments to Lenders                                    | (1,470,965)         | (2,116,250)         |
| Adjustment Due to Reestimate & Guarantied Loan Purchases     | 650,340             | 577,925             |
| Miscellaneous Recoveries and Costs                           | (11,765)            | 10,088              |
| Balance of Liability for Loan Guaranties before Reestimates  | 3,506,675           | 3,715,252           |
| Technical Assumptions/Default Reestimates                    | (1,462,236)         | (728,034)           |
| <b>Ending Balance of Liability for Loan Guaranties</b>       | <b>2,044,439</b>    | <b>2,987,218</b>    |
| <b>Total Ending Balance of Liability for Loan Guaranties</b> | <b>\$ 2,044,509</b> | <b>\$ 2,987,263</b> |

## F. FY 2014 Subsidy Rates by Program and Component

| LOAN PROGRAM                  | Total Subsidy | Financing | Default | Other  | Fee    |
|-------------------------------|---------------|-----------|---------|--------|--------|
| <b>Guaranty</b>               |               |           |         |        |        |
| 7(a) (10-1-13 to 12-31-13)    | <b>0.00%</b>  | 0.00%     | 3.98%   | 0.00%  | -3.98% |
| 7(a) (1-1-14 to 9-30-14)      | <b>0.01%</b>  | 0.00%     | 3.98%   | 0.00%  | -3.97% |
| 504 CDC                       | <b>1.71%</b>  | 0.00%     | 8.91%   | 0.97%  | -8.17% |
| SBIC Debentures               | <b>0.00%</b>  | 0.00%     | 5.07%   | 0.12%  | -5.19% |
| <b>Direct</b>                 |               |           |         |        |        |
| Disaster (10-1-13 to 4-24-14) | <b>8.48%</b>  | -2.52%    | 15.10%  | -4.10% | 0.00%  |
| Disaster (4-25-14 to 9-30-14) | <b>8.53%</b>  | -2.52%    | 15.16%  | -4.11% | 0.00%  |
| Microloan                     | <b>18.64%</b> | 8.19%     | 1.88%   | 8.57%  | 0.00%  |

The subsidy rates in Table F pertain only to loans obligated in the current year. These rates cannot be applied to the loans disbursed during the current year to yield the subsidy expense because loans disbursed during the current year include loans obligated in prior years. In FY 2014, the subsidy rate for the 7(a) loan program was adjusted due to the introduction of fee relief for loans under \$150,000 and the subsidy rate for the Disaster loan program was adjusted due to a change in collateral requirements. Subsidy expenses reported in Table G result from the disbursement of loans obligated in the current year as well as in prior years, and include reestimates.

## G. Subsidy Expense by Component

(Dollars in Thousands)

| For the Years Ending September 30,                        | 2014                  | 2013                |
|---|-----------------------|---------------------|
| <b>Business Loan Guaranties</b>                           |                       |                     |
| Interest  | \$ 39                 | \$ (44)             |
| Defaults  | 971,685               | 1,493,312           |
| Fees  | (857,676)             | (1,250,050)         |
| Other   | 29,819                | 32,524              |
| Subsidy Expense Before Reestimates and Loan Modifications | 143,867               | 275,742             |
| Reestimates   | (1,462,236)           | (728,034)           |
| <b>Total Guaranteed Business Loan Subsidy Expense</b>     | <b>\$ (1,318,369)</b> | <b>\$ (452,292)</b> |
| <b>Business Direct Loans</b>                              |                       |                     |
| Interest  | \$ 3,227              | \$ 5,130            |
| Defaults  | 758                   | 1,024               |
| Other   | 2,572                 | 2,156               |
| Subsidy Expense Before Reestimates                        | 6,557                 | 8,310               |
| Reestimates   | (6,614)               | (23,277)            |
| <b>Total Business Direct Loan Subsidy Expense</b>         | <b>\$ (57)</b>        | <b>\$ (14,967)</b>  |
| <b>Disaster Direct Loans</b>                              |                       |                     |
| Interest  | \$ 4,964              | \$ 28,438           |
| Defaults  | 61,760                | 108,852             |
| Other   | (22,330)              | (46,617)            |
| Subsidy Expense Before Reestimates                        | 44,394                | 90,673              |
| Reestimates   | 6,563                 | (2,068)             |
| <b>Total Disaster Direct Loan Subsidy Expense</b>         | <b>\$ 50,957</b>      | <b>\$ 88,605</b>    |

## H. Administrative Expense

The SBA received appropriations to administer its credit programs, including the making, servicing, and liquidation of its loans and guaranties. Amounts expensed in the Statement of Net Cost are:

(Dollars in Thousands)

| For the Years Ending September 30,  | 2014              | 2013              |
|-------------------------------------|-------------------|-------------------|
| Disaster Direct Loan Programs       | \$ 177,469        | \$ 273,718        |
| Business Loan Programs              | 151,282           | 142,044           |
| <b>Total Administrative Expense</b> | <b>\$ 328,751</b> | <b>\$ 415,762</b> |

## I. Credit Program Subsidy Reestimates

Reestimates are performed annually, on a cohort-by-cohort basis. The purpose of reestimates is to update original program cost estimates to reflect actual cash flow experience as well as changes in forecasts of future cash flows. Forecasts of future cash flows are updated based on additional information about historical program performance, revised expectations for future economic conditions, and enhancements to cash flow projection methods. Financial statement reestimates were performed using a full year of performance data for FY 2014 for SBA's large loan programs and with nine months of actual and three months of projected performance data for the Secondary Market Guaranty and the small loan programs.

## BUSINESS GUARANTIED LOAN PROGRAMS

Net subsidy reestimates for the business guaranteed loan programs follows.

(Dollars in Thousands)

| For the Years Ending September 30,                       | 2014                  | 2013                |
|--|-----------------------|---------------------|
| 7(a)   | \$ (327,206)          | \$ (391,029)        |
| 7(a) - Recovery Act                                      | 398                   | (44,930)            |
| 7(a) - Jobs Act  | (54,904)              | (78,740)            |
| Dealer Floor Plan  | (1,866)               | (937)               |
| 504 CDC  | (619,688)             | (128,079)           |
| 504 CDC - Recovery Act                                   | (120,036)             | (112,787)           |
| 504 CDC - Jobs Act                                       | (33,148)              | (29,298)            |
| 504 CDC - Debt Refinancing                               | (87,334)              | (1,308)             |
| 504 First Mortgage Loan Pooling - Recovery Act           | 1,726                 | (4,924)             |
| SBIC Debentures  | (53,499)              | 31,577              |
| SBIC Participating Securities                            | (96,055)              | 48,388              |
| Secondary Market Guaranty Program                        | (61,915)              | 7,980               |
| ARC - Recovery Act                                       | (15,131)              | (22,434)            |
| All Other Guaranty Loan Programs                         | 6,422                 | (1,513)             |
| <b>Total Guaranteed Loan Program Subsidy Reestimates</b> | <b>\$ (1,462,236)</b> | <b>\$ (728,034)</b> |

The 7(a) Loan Guaranty program, SBA's flagship and largest program had a net downward reestimate in FY 2014 of \$327.2 million. The reestimate is primarily due to better than expected loan performance in cohorts 2011 through 2014, offsetting worse than expected loan performance in cohorts 2005 through 2010. Strong loan performance was driven by lower than projected purchases in cohorts 2011 through 2014. Actual purchases for these cohorts were less than half of the purchases projected during FY 2014. The remainder of the reestimate is due to decreased loss projection for the 2014 cohort as compared to the original loss projections.

The 7(a) Recovery Act program had a net upward reestimate in FY 2014 of \$0.4 million. Lower than expected purchases in FY 2014 were offset by lower than expected recoveries. Additionally, FY 2014 loan performance contributed to updated model assumptions, which resulted in decreased recovery projections.

The 7(a) Jobs Act cohort had a net downward reestimate in FY 2014 of \$54.9 million. A significant portion of the reestimate is due to significantly better than projected FY 2014 loan performance. Actual purchases in the 7(a) Jobs Act cohort during FY 2014 were less than half of the purchases projected for FY 2014.

The Dealer Floor Plan program had a net downward reestimate of \$1.9 million due to better than projected performance during FY 2014 and a technical adjustment to the treatment of the revolving lines of credit in accordance with changes in the guidance presented in OMB Circular A-11.

The 504 Certified Development Company program had a net downward reestimate of \$619.7 million. The reestimate is primarily due to better than projected FY 2014 loan performance across all cohorts. Although some cohorts had higher than expected purchases, these unexpected losses were offset by higher than expected recoveries in all cohorts. The remainder of the reestimate was due to decreased loss projections for the 2014 cohort as compared to the original loss projections.

The 504 Recovery Act program had a net downward reestimate of \$120 million. The reestimate is due to better than projected FY 2014 loan performance. Actual purchases in the 504 Recovery Act program were less than a quarter of the purchases projected for FY 2014.

The 504 Jobs Act program had a net downward reestimate of \$33.1 million. The reestimate is due to better than projected FY 2014 loan performance. Actual purchases in the 504 Jobs Act program were less than a quarter of the purchases projected for FY 2014.

The 504 Debt Refinancing program had a net downward reestimate of \$87.3 million. The reestimate is due to better than projected FY 2014 loan performance. Actual purchases in the 504 Debt Refinancing program were less than a quarter of the purchases projected for FY 2014.

The Section 504 First Mortgage Loan Pooling program had a net upward reestimate of \$1.7 million. Lower than projected purchases in all three cohorts in FY 2014 were offset by lower than expected recoveries. Additionally, FY 2014 loan performance contributed to updated model assumptions, which resulted in decreased recovery projections.

The SBIC Debentures program had a net downward reestimate of \$53.5 million. The primary driver of the reestimate was better than projected loan performance in FY 2014. Actual purchases were less than projected for FY 2014. Additionally, FY 2014 loan performance contributed to updated model assumptions, which resulted in decreased cash outflow projections.

The SBIC Participating Securities program had a net downward reestimate of \$96.1 million. The downward reestimate was due to better than expected loan performance in FY 2014, particularly for the 2001-2004 cohorts. Actual recoveries were higher than projected and actual purchases were lower than projected in FY 2014. This was partially offset by lower actual reimbursements of prioritized payments than projected in FY 2014.

The Secondary Market Guaranty program had a net downward reestimate of \$61.9 million. This downward reestimate was driven mainly by updating the forecasted pool balances in the Master Reserve Fund with the actual balances. The actual MRF balances were higher than previously projected, resulting in lower cash outflows to cover future SMG pool obligations.

The America’s Recovery Capital program had a net downward reestimate of \$15.1 million. The majority of this reestimate is due to better than projected loan performance in FY 2014. The remainder of the reestimate is mostly due to lower purchase projections in future years as a result of recent actual loan performance.

**BUSINESS DIRECT LOAN PROGRAMS**

Net subsidy reestimates for business direct loan programs follows.

*(Dollars in Thousands)*

| For the Years Ending September 30,                   | 2014              | 2013               |
|--|-------------------|--------------------|
| 7(m) Microloan                                       | \$ (3,412)        | \$ (17,653)        |
| 7(m) Microloan - Recovery Act                        | (1,030)           | (4,719)            |
| Intermediary Lending Pilot Program                   | (73)              | (1,148)            |
| SBIC Preferred Stock                                 | (2,095)           | 289                |
| All Other Direct Loan Programs                       | (4)               | (46)               |
| <b>Total Direct Loan Program Subsidy Reestimates</b> | <b>\$ (6,614)</b> | <b>\$ (23,277)</b> |

The 7(m) Direct Microloan program had a net downward reestimate of \$3.4 million. The downward reestimate is due partly to decreased projected losses in future years, especially for cohorts 2001, 2004-2005, 2007-2008, and 2011-2012. Additionally, increases in actual interest collected during FY 2014 and projected interest collections for all remaining years of most cohorts factored into the downward reestimate.

The 7(m) Direct Microloan Recovery Act program had a net downward reestimate of \$1.0 million. The downward reestimate is primarily due to decreased projected losses in future years, especially in the 2010 cohort.

The Intermediary Lending Pilot program had a modest net downward reestimate of \$0.1 million. For both the 2011 and 2012 cohorts, an increase in actual interest collected during FY 2014 and projected interest collections for all remaining years slightly offset increases in loss projections related to loan performance to generate the modest net downward reestimate.

## DISASTER DIRECT LOAN PROGRAM

Net subsidy reestimates for the disaster direct loan programs follows:

*(Dollars in Thousands)*

| <b>For the Years Ending September 30,</b>                     | <b>2014</b>     | <b>2013</b>       |
|---|-----------------|-------------------|
| Disaster  | \$ 6,563        | \$ (2,068)        |
| <b>Total Disaster Direct Loan Program Subsidy Reestimates</b> | <b>\$ 6,563</b> | <b>\$ (2,068)</b> |

The Disaster Assistance program had a net upward reestimate of \$6.6 million. The 2006 and 2014 cohorts experienced the largest upward reestimates, while the 2007 and 2013 cohorts experienced the largest downward reestimates. The upward reestimate for the 2006 cohort was due to worse than expected performance in FY 2014 and due to updated projections of future performance, while the upward reestimate for the 2014 cohort was due to the actual average borrower's interest rate being lower than the original projected average borrower's interest rate. The downward reestimate for the 2007 cohort was due to better than expected performance in FY 2014, while the downward reestimate for the 2013 cohort was due to updated present value discount factors applied to projected cash flows.

## NOTE 7 GENERAL PROPERTY AND EQUIPMENT, NET

The SBA capitalizes equipment with a cost of \$50,000 or more per unit and a useful life of 2 years or more at full cost and depreciates using the straight-line method over the useful life. The SBA expenses equipment not meeting the capitalization criteria.

Leasehold improvements with modifications of \$50,000 or more and a useful life of 2 years or more are capitalized and amortized using the straight-line method over the useful life of the improvement or the lease term, whichever is shorter. Leasehold improvements not meeting the capitalization criteria are expensed.

Software intended for internal use, whether internally developed, contractor developed, or purchased, is capitalized at cost if the unit acquisition cost is \$250,000 or more and service life is at least 2 years. Capitalized software costs include all direct and indirect costs incurred, including overhead to develop the software. Software for internal use is amortized using the straight-line method over its useful life, not to exceed 5 years. Amortization begins when the software is put into production. The costs of enhancements are capitalized when it is more likely than not that the enhancements will result in significant additional capabilities. Costs that do not meet the capitalization criteria are expensed when incurred.

Assets meeting the capitalization thresholds are detailed here.

(Dollars in Thousands)

| As of September 30,                              | 2014            | 2013            |
|--|-----------------|-----------------|
| Equipment  | \$ 2,675        | \$ 2,675        |
| Accumulated Depreciation                         | (2,491)         | (2,183)         |
| <b>Net</b>                                       | <b>184</b>      | <b>492</b>      |
| Leasehold Improvements                           | 1,811           | 1,811           |
| Amortization of Leasehold Improvements           | (853)           | (702)           |
| <b>Net</b>                                       | <b>958</b>      | <b>1,109</b>    |
| Software in Development                          | -               | 4,572           |
| Software in Use                                  | 35,926          | 30,546          |
| Amortization of Software in Use                  | (32,339)        | (30,546)        |
| <b>Net</b>                                       | <b>3,587</b>    | <b>4,572</b>    |
| <b>Total General Property and Equipment, Net</b> | <b>\$ 4,729</b> | <b>\$ 6,173</b> |

## NOTE 8 LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

Liabilities not covered by budgetary resources are liabilities for which congressional action is needed before budgetary resources can be provided. These unfunded liabilities consisted of:

(Dollars in Thousands)

| As of September 30,  | 2014              | 2013             |
|--|-------------------|------------------|
| <b>Intragovernmental Liabilities - Other</b>                   |                   |                  |
| Employment Taxes Payable                                       | \$ 1,536          | \$ 1,496         |
| Federal Employees' Compensation Act Payable                    | 6,026             | 5,854            |
| <b>Total Intragovernmental Liabilities - Other</b>             | <b>7,562</b>      | <b>7,350</b>     |
| <b>Federal Employees' Compensation Act Actuarial Liability</b> | <b>34,627</b>     | <b>33,703</b>    |
| <b>Surety Bond Guarantee Program Future Claims</b>             | <b>35,799</b>     | <b>31,029</b>    |
| <b>Other Liabilities</b>                                       |                   |                  |
| Prior Liens on Real Estate Payable                             | 59                | 59               |
| Accrued Unfunded Annual Leave                                  | 26,361            | 26,871           |
| <b>Total Other Liabilities</b>                                 | <b>26,420</b>     | <b>26,930</b>    |
| <b>Total Liabilities Not Covered by Budgetary Resources</b>    | <b>\$ 104,408</b> | <b>\$ 99,012</b> |

The liability for Surety Bond Guarantees is an estimate of future claims in the SBG program for guaranties outstanding at year-end.

**NOTE 9 DEBT**

Borrowings payable to the Treasury result from loans provided by the Treasury to fund the portion of direct loans not covered by subsidy appropriations and to fund the payment of downward subsidy reestimates and other credit program disbursements (see Note 15). The SBA makes periodic principal repayments to the Treasury based on the analysis of its cash balances and future disbursement needs.

Borrowings payable to the Federal Financing Bank are the result of its financing of SBA Section 503 Debentures issued prior to 1988.

All debt is intragovernmental and covered by budgetary resources. Debt transactions for the periods ending September 30, 2014 and 2013 and resulting balances are:

**INTRAGOVERNMENTAL DEBT**

*(Dollars in Thousands)*

| <b>As of September 30,</b>    | <b>2014</b>         | <b>2013</b>         |
|-------------------------------|---------------------|---------------------|
| <b>Department of Treasury</b> |                     |                     |
| <b>Beginning Balance</b>      | <b>\$ 8,088,099</b> | <b>\$ 7,919,741</b> |
| New Borrowing                 | 852,468             | 1,320,219           |
| Repayments                    | (1,184,467)         | (1,151,861)         |
| <b>Ending Balance</b>         | <b>\$ 7,756,100</b> | <b>\$ 8,088,099</b> |
| <b>Federal Financing Bank</b> |                     |                     |
| <b>Beginning Balance</b>      | <b>\$ -</b>         | <b>\$ 60</b>        |
| Repayments                    | -                   | (58)                |
| Change in Interest Payable    | -                   | (2)                 |
| <b>Ending Balance</b>         | <b>\$ -</b>         | <b>\$ -</b>         |
| <b>Total Debt</b>             | <b>\$ 7,756,100</b> | <b>\$ 8,088,099</b> |

**NOTE 10 NET ASSETS OF LIQUIDATING FUNDS DUE TO TREASURY**

Net Assets of Liquidating Funds Due to Treasury is the residual of the book value of assets less liabilities in the Liquidating Funds for loans made prior to FY 1992. The FY 2013 balance includes the unobligated balance for budgetary reporting that was transferred to the Treasury in early FY 2014. In FY 2014, the SBA developed procedures to transfer the unobligated balance at September 30 instead of in the following fiscal year.

*(Dollars in Thousands)*

| <b>As of September 30,</b>                | <b>2014</b>      | <b>2013</b>      |
|---|------------------|------------------|
| Pollution Control Equipment Guaranty Fund | \$ -             | \$ 1,119         |
| Disaster Loan Fund                        | 3,297            | 8,148            |
| Business Loan and Investment Fund         | 6,843            | 32,431           |
| <b>Total Due Treasury</b>                 | <b>\$ 10,140</b> | <b>\$ 41,698</b> |

## NOTE 11 OTHER LIABILITIES

Other liabilities were:

(Dollars in Thousands)

| As of September 30,                                | 2014             | 2013             |
|--|------------------|------------------|
| <b>OTHER LIABILITIES - INTRAGOVERNMENTAL</b>       |                  |                  |
| <b>Entity</b>                                      |                  |                  |
| <b>Current</b>                                     |                  |                  |
| Employment Taxes Payable                           | \$ 2,084         | \$ 1,817         |
| Advances from Other Agencies                       | 332              | 478              |
| <b>Total Current</b>                               | <b>2,416</b>     | <b>2,295</b>     |
| <b>Non-current</b>                                 |                  |                  |
| Employment Taxes Payable                           | 1,536            | 1,496            |
| Federal Employees' Compensation Act Payable        | 6,026            | 5,854            |
| <b>Total Non-current</b>                           | <b>7,562</b>     | <b>7,350</b>     |
| <b>Total Entity</b>                                | <b>9,978</b>     | <b>9,645</b>     |
| <b>Non-entity</b>                                  |                  |                  |
| <b>Current</b>                                     |                  |                  |
| Payable to Treasury                                | 6                | 7                |
| <b>Total Other Liabilities - Intragovernmental</b> | <b>\$ 9,984</b>  | <b>\$ 9,652</b>  |
| <b>OTHER LIABILITIES - PUBLIC</b>                  |                  |                  |
| <b>Entity</b>                                      |                  |                  |
| <b>Current</b>                                     |                  |                  |
| Accrued Funded Payroll and Benefits                | \$ 13,778        | \$ 7,753         |
| Accrued Unfunded Annual Leave                      | 26,361           | 26,871           |
| Contingent Liability                               | 464              | -                |
| Suspense Accounts                                  | 1,128            | 189              |
| <b>Total Current</b>                               | <b>41,731</b>    | <b>34,813</b>    |
| <b>Non-current</b>                                 |                  |                  |
| Prior Liens on Real Estate Payable                 | 59               | 59               |
| <b>Total Non-current</b>                           | <b>59</b>        | <b>59</b>        |
| <b>Total Entity</b>                                | <b>41,790</b>    | <b>34,872</b>    |
| <b>Non-entity</b>                                  |                  |                  |
| <b>Current</b>                                     |                  |                  |
| Non-entity Current Payable                         | -                | 4                |
| <b>Total Other Liabilities - Public</b>            | <b>\$ 41,790</b> | <b>\$ 34,876</b> |

## NOTE 12 LEASES

The SBA leases all of its facilities from the General Services Administration. The SBA enters into an Occupancy Agreement with GSA for each facility. GSA, in turn, leases commercial facilities or provides space in federal buildings. Agreements for space in federal buildings can be vacated with 120 to 180 days notice. However, the SBA anticipates continuing the same or similar facilities leases in the future. These leases with GSA are operating leases and are expensed in the Statement of Net Cost when incurred. FY 2014 and 2013 facilities lease costs were \$45.1 million and \$44.7 million. Future lease payments shown here assume a 3 percent inflation factor from the following years' projected totals as estimated by GSA, as well as continued costs during the next 5 years as leases expire and new leases are added. Payments after 5 years reflect only current leases that will still be in effect then, projected to the end of each lease term.

**FUTURE FACILITIES OPERATING LEASE PAYMENTS***(Dollars in Thousands)*

| <b>Fiscal Year</b> | <b>Lease Payments</b> |
|--------------------|-----------------------|
| 2015               | \$ 44,846             |
| 2016               | 46,191                |
| 2017               | 47,577                |
| 2018               | 49,004                |
| 2019               | 50,474                |
| After 2019         | 36,186                |
| <b>Total</b>       | <b>\$ 274,278</b>     |

**NOTE 13 NON-ENTITY REPORTING**

Non-entity Assets are assets held by the SBA but not available to the SBA. The primary non-entity asset is for SBA's downward subsidy reestimates in its loan programs. Because the loan programs are discretionary, the downward reestimates are not available to the SBA and they are returned to the Treasury in the fiscal year following the accrual of the reestimates. During the year, these general fund accounts contain SBA's prior year reestimates. At year-end, the funds are swept by the Treasury. Also at year-end, the SBA accrues the current year's reestimates, including downward reestimates as applicable. For the downward reestimates, in the loan financing funds, the SBA records an accrual adjustment that records a transfer out to the non-entity fund, a reduction of subsidy allowance or loan guarantee liability, and an account payable to the non-entity fund. In the loan program funds the SBA records a reduction of loan subsidy expense and the associated impact on the net cost. The non-entity Treasury general funds contain a corresponding account receivable in anticipation of the receipt of the downward reestimates in the following year and a Downward Reestimate Payable to the Treasury.

For consolidated financial statement presentation, the SBA eliminates the payable to the non-entity fund and the non-entity Treasury general fund receivable from the financing funds; since both are included in SBA's reporting entity. The Downward Reestimate Payable to the Treasury in the non-entity Treasury general fund is not eliminated and is reflected on the Balance Sheet as a liability line item.

*(Dollars in Thousands)*

| <b>As of September 30,</b>              | <b>2014</b>           | <b>2013</b>           |
|---|-----------------------|-----------------------|
| <b>Entity</b>                           |                       |                       |
| Financing Fund Payable                  | \$ (1,637,283)        | \$ (1,116,192)        |
| <b>Non-entity</b>                       |                       |                       |
| Miscellaneous Receipts Fund Receivable  | 1,637,283             | 1,116,192             |
| Downward Reestimate Payable to Treasury | (1,637,283)           | (1,116,192)           |
| <b>Balance Sheet Reported Payable</b>   | <b>\$ (1,637,283)</b> | <b>\$ (1,116,192)</b> |

## NOTE 14 CONSOLIDATED STATEMENT OF NET COST

Federal cost accounting standards require the SBA to report operating costs by strategic goal activity. Full costs include all direct and indirect costs for a strategic goal. Full costs are reduced by exchange (earned) revenues to arrive at net operating cost.

### Operating Cost

The full and net operating costs of SBA's strategic goals are presented in the Consolidated Statement of Net Cost. Full costs are comprised of all direct costs for the strategic goals and those indirect costs which can be reasonably assigned or allocated to the strategic goals, including employee pension and other retirement benefit costs paid by the OPM and charged to the SBA.

### Earned Revenue

Earned revenue arises from exchange transactions, and is deducted from the full cost of SBA's strategic goals to arrive at net strategic goals costs. The SBA recognizes earned revenue when reimbursements are payable from other federal agencies and the public, as a result of costs incurred or services performed. A major source of earned revenue includes interest earned on SBA's outstanding Business and Disaster loan portfolios and interest earned on uninvested funds in the credit reform financing accounts.

### Reporting by Strategic Goal

The SBA reports net costs consistent with its three strategic goals on a full cost allocation basis. The SBA issued its *FY 2014-2018 Strategic Plan* this year, and FY 2013 costs have been reclassified to be comparable to the new strategic goal architecture. Strategic Goal 1 (Growing Businesses and Creating Jobs) includes SBA's loan, disaster, and other assistance programs, and now includes STEP grants that were excluded in the previous strategic plan. Strategic Goal 2 (Serving as the Voice for Small Business) is similar to the previous Strategic Goal 3 that includes small business advocacy, and now includes programs to promote entrepreneurship in economic sectors and communities where market gaps remain that were in the previous Strategic Goal 1. Strategic Goal 3 (Building an SBA that Meets the Needs of Today's and Tomorrow's Small Businesses) is similar to the previous Strategic Goal 2 and now includes lender oversight costs that were in the previous Strategic Goal 1. Agency administrative overhead costs are fully allocated to the programs in Strategic Goals 1, 2, and 3. The Management's Discussion and Analysis section of SBA's annual Agency Financial Report includes additional detail on SBA's strategic goals. Costs Not Assigned to Strategic Goals include the Office of the Inspector General and grants made under congressionally mandated programs. The Office of the Inspector General's mission and funding is independent of SBA's and is therefore excluded. Congressional mandated grants do not necessarily involve small business and are also excluded.

Intragovernmental Gross Cost is incurred by the SBA in exchange transactions with other federal agencies, and Gross Cost with the Public is incurred in exchange transactions with the Public. Intragovernmental Earned Revenue is earned by the SBA in exchange transactions with other federal agencies, and Earned Revenue from the Public is earned in exchange transactions with the Public. The General Services Administration and the Treasury Department are SBA's primary Intragovernmental trading partners.

The classification as Intragovernmental Costs or Gross Cost with the Public relate to the source of goods and services received by the SBA and not to the classification of related revenue. The classification of revenue or cost being defined as "intragovernmental" or "public" is defined on a transaction by transaction basis. The purpose of this classification is to enable the federal government to provide consolidated financial statements, and not to match the public and intragovernmental revenue with costs that are incurred to produce public and intragovernmental revenue.

SBA's Gross Cost with the Public in Strategic Goal 1 is largely determined by estimates and reestimates of its credit program costs (See Note 6I). Downward reestimates of these costs caused the credit to Gross Cost with the Public in FY 2014.

## INTRAGOVERNMENTAL COSTS AND EXCHANGE REVENUE

*(Dollars in Thousands)*

| For the Years Ended September 30,  | 2014                | 2013              |
|--|---------------------|-------------------|
| <b>STRATEGIC GOAL 1:</b>   |                     |                   |
| <b>Growing Businesses and Creating Jobs</b>  |                     |                   |
| Intragovernmental Gross Cost   | \$ 506,417          | \$ 524,105        |
| Gross Cost with the Public   | (613,675)           | 477,945           |
| <b>Total Strategic Goal 1 Gross Cost</b>   | <b>(107,258)</b>    | <b>1,002,050</b>  |
| Intragovernmental Earned Revenue   | 138,871             | 166,677           |
| Earned Revenue from the Public   | 372,857             | 447,918           |
| <b>Total Strategic Goal 1 Earned Revenue</b>   | <b>511,728</b>      | <b>614,595</b>    |
| <b>STRATEGIC GOAL 2:</b>   |                     |                   |
| <b>Serving as the Voice for Small Business</b>   |                     |                   |
| Intragovernmental Gross Cost   | \$ 26,178           | \$ 18,930         |
| Gross Cost with the Public   | 83,310              | 74,034            |
| <b>Total Strategic Goal 2 Gross Cost</b>   | <b>109,488</b>      | <b>92,964</b>     |
| <b>STRATEGIC GOAL 3:</b>   |                     |                   |
| <b>Building an SBA that Meets the Needs of Today's and Tomorrow's Small Businesses</b> |                     |                   |
| Intragovernmental Gross Cost   | \$ 6,176            | \$ 1,203          |
| Gross Cost with the Public   | 19,654              | 4,705             |
| <b>Total Strategic Goal 3 Gross Cost</b>   | <b>25,830</b>       | <b>5,908</b>      |
| <b>COST NOT ASSIGNED TO STRATEGIC GOALS</b>  |                     |                   |
| Intragovernmental Gross Cost   | \$ 4,130            | \$ 7,689          |
| Gross Cost with the Public   | 13,144              | 30,070            |
| <b>Total Gross Cost Not Assigned to Strategic Goals</b>                                | <b>17,274</b>       | <b>37,759</b>     |
| <b>Net Cost of Operations</b>  | <b>\$ (466,394)</b> | <b>\$ 524,086</b> |

**NOTE 15 STATEMENT OF BUDGETARY RESOURCES**

The Statement of Budgetary Resources presents information about total budgetary resources available to the SBA and the status of those resources as of September 30, 2014 and 2013. SBA's total budgetary resources were \$3.0 billion and \$4.2 billion for the years ended September 30, 2014 and 2013. Additionally, \$7.8 billion and \$9.9 billion of nonbudgetary resources including borrowing authority and collections of loan principal, interest and fees in financing funds were reported for the years ended September 30, 2014 and 2013.

**Permanent Indefinite Appropriations**

The SBA receives permanent indefinite appropriations annually to fund increases in the projected subsidy costs of loan programs as determined by the reestimation process required by the Federal Credit Reform Act of 1990. The appropriations are received initially in the SBA Program Funds and then transferred to the Financing Funds where they are used to fund obligations. SBA's Liquidating Funds also receive permanent indefinite appropriations to fund obligations. The Financing Funds are used to account for credit program obligations made subsequent to FY 1991. Liquidating Funds are used to account for credit program obligations made prior to FY 1992.

Decreases in projected subsidy costs in the Financing Funds are returned to the Treasury through SBA's annual reestimation process. The prior year's ending unobligated balances in SBA's Liquidating Funds are also transferred to the Treasury annually.

## Borrowing Authority and Terms of Borrowing

The SBA is authorized to borrow from the Treasury's Bureau of the Fiscal Service when funds needed to disburse direct loans and purchase guaranteed loans exceed subsidy costs and collections in the nonbudgetary loan financing funds. In FY 2014 and FY 2013, the SBA received \$0.8 billion and \$1.5 billion of borrowing authority from the OMB. At the end of FY 2014, the SBA had \$0.2 billion in borrowing authority carried over to fund direct loans and default claims to be disbursed in the future. At the end of FY 2013, the SBA had \$0.3 billion in available borrowing authority. The SBA pays interest to the Treasury based on Treasury's cost of funds. The rate at which interest is paid to the Treasury on the amounts borrowed (or received from the Treasury on uninvested cash balances) in a loan financing fund for a particular cohort is a disbursement-weighted average discount rate for cohorts prior to FY 2001 and a single effective rate for cohorts beginning with FY 2001. The SBA calculates and repays borrowings not needed for working capital at midyear for prior year cohorts. The SBA uses the loan principal, interest and fees collected from the borrowers in its loan financing funds to repay its Treasury borrowings. The repayment maturity dates for the borrowing from the Treasury are based on the loan maturities used in the subsidy calculation. The maturities range from 16 years for Direct Business loans, 25 years for Guaranteed Business loans and 30 years for Disaster loans.

## Apportionment Categories of Obligations Incurred

During FY 2014 and FY 2013, the SBA incurred \$5.1 billion and \$8.6 billion of direct and reimbursable obligations of which \$0.0 billion and \$0.6 billion was apportioned in category A; \$5.1 billion and \$8.0 billion was apportioned in category B. Category A apportionments are restricted by quarter and program; category B apportionments are restricted by purpose and program.

## Unobligated Balances

Unobligated balances at September 30, 2014 and 2013 are \$5.7 billion and \$5.4 billion which include \$3.7 billion and \$4.0 billion of unavailable unobligated balances. These balances are unavailable primarily because they are unapportioned by the OMB. The SBA accumulates the majority of these unobligated balances in its nonbudgetary financing accounts during the fiscal year (\$4.3 billion in FY 2014 and \$4.1 billion in FY 2013) from reestimates that are used primarily to pay default claims in the following fiscal year. In addition, unobligated balances are accumulated in budgetary accounts from appropriations (\$1.4 billion in FY 2014 and \$1.3 billion in FY 2013) that are used to finance SBA's ongoing program operations. The SBA requests OMB apportionments as needed, and after OMB approval, apportioned amounts are available for obligation.

## Undelivered Orders

Undelivered orders are obligations that have not yet been disbursed by the SBA. Undelivered orders for the periods ended September 30, 2014 and 2013 were \$0.6 billion and \$1.2 billion.

## Differences between the Statement of Budgetary Resources and the Budget of the U. S. Government

There was no material difference between the FY 2013 Statement of Budgetary Resources and the President's FY 2015 budget submission. The President's Budget with actual numbers for FY 2016 has not yet been published. The SBA expects no material differences between the President's Budget "actual" column and the FY 2014 reported results when the budget becomes available in February 2015.

## NOTE 16 RECONCILIATION OF BUDGETARY OBLIGATIONS INCURRED TO NET COST OF OPERATIONS

The SBA presents the Statement of Net Cost using the accrual basis of accounting. This differs from the obligation-based measurement of total resources supplied, both budgetary and from other sources, on the Statement of Budgetary Resources.

The Federal Financial Accounting Standard No. 7 requires “a reconciliation of proprietary and budgetary information in a way that helps users relate the two.” The focus of this presentation is to reconcile budgetary net obligations to the net cost of operations. The objective of this information is to categorize the differences between budgetary and financial (proprietary) accounting.

### SUCCESS STORY: Bold Ideas and Customer Focus Pay Off

Myers-Seth Pump, Jacksonville, Florida

**Teresa Myers**, an immigrant from Vietnam, is CEO of Myers-Seth Pump (MSP), a company that manufactures pumps and dewatering equipment throughout the United States and abroad. She and her husband, **Douglas Myers**, jointly own and operate the 14-year-old company.

MSP has faced its share of challenges. As a manufacturer of industrial and construction pumps for mining and construction industries, MSP was impacted by the economic crisis of 2009. Teresa Myers navigated through the recession by adding a pump rental division, providing training opportunities for her employees, and expanding the company’s outreach to other industries, such as the oil and gas industry, and international markets. Another challenge was a set of fires that occurred onsite at their facility. The fires occurred during MSP’s busiest production season, but the company was able to continue with very little interruption. In fact, most of MSP’s customers were not even aware that they had a major fire. MSP also increased its revenue by almost 20 percent when it started exporting pumps overseas.

Teresa attributes her success to hard work, customer focus, and to the training she received as part of SBA’s Emerging Leaders program. “Participating in the Emerging Leaders program gave me the most in-depth knowledge on how to effectively run a small business. I learned about structuring the business, profitability, planning, creating exit strategies, and scaling my business,” she said. Teresa Myers also participated in SBA resource partner training and development programs through the Jacksonville Women’s Business Center and the Small Business Development Center at the University of North Florida.



## CONSOLIDATED RECONCILIATION OF BUDGETARY OBLIGATIONS TO NET COST

*(Dollars in Thousands)*

| <b>For the Years Ended September 30,</b>  | <b>2014</b>         | <b>2013</b>        |
|---|---------------------|--------------------|
| <b>RESOURCES USED TO FINANCE ACTIVITIES</b>   |                     |                    |
| <b>Budgetary Resources Obligated</b>  |                     |                    |
| Obligations Incurred  | \$ 5,114,412        | \$ 8,625,608       |
| Less: Spending Authority from Offsetting Collections and Recoveries   | 4,584,340           | 5,431,669          |
| Obligations Net of Offsetting Collections and Recoveries  | 530,072             | 3,193,939          |
| Less: Offsetting Receipts   | 1,123,155           | 1,696,979          |
| <b>Net Obligations</b>  | <b>(593,083)</b>    | <b>1,496,960</b>   |
| <b>Other Resources</b>  |                     |                    |
| Imputed Financing   | 21,893              | 19,955             |
| Other Financing Sources   | (1,648,365)         | (1,127,912)        |
| <b>Net Other Resources Used to Finance Activities</b>   | <b>(1,626,472)</b>  | <b>(1,107,957)</b> |
| <b>Total Resources Used to Finance Activities</b>   | <b>(2,219,555)</b>  | <b>389,003</b>     |
| <b>RESOURCES THAT DO NOT FINANCE NET COST OF OPERATIONS</b>   |                     |                    |
| (Increase) Decrease in Budgetary Resources Obligated for Goods, Services,<br>and Benefits Ordered But Not Yet Provided  | 450,569             | (371,232)          |
| Resources that Fund Expenses Recognized in Prior Periods  | (362,689)           | (882,703)          |
| Budgetary Offsetting Collections and Receipts that Do Not Affect Net Cost of Operations                                 |                     |                    |
| Credit Program Collections  | 3,923,558           | 4,540,597          |
| Offsetting Receipts   | 1,123,155           | 1,696,979          |
| Resources that Finance the Acquisition of Assets or Liquidation of Liabilities  | (3,591,420)         | (5,224,054)        |
| Other - Current Year Liquidating Equity Activity  | 3,218               | 3,992              |
| Other Resources that Do Not Affect Net Cost of Operations   | 38                  | (27)               |
| <b>Total Resources that Do Not Finance Net Cost of Operations</b>   | <b>1,546,429</b>    | <b>(236,448)</b>   |
| <b>Total Resources Used to Finance the Net Cost of Operations</b>   | <b>(673,126)</b>    | <b>152,555</b>     |
| <b>COMPONENTS OF THE NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD</b>       |                     |                    |
| <b>Components Requiring or Generating Resources in Future Periods</b>   |                     |                    |
| Change in Annual Leave Liability  | (510)               | 1,113              |
| Change in Contingent Liability  | 464                 | -                  |
| Upward Reestimates of Credit Subsidy Expense  | 200,923             | 362,329            |
| Change in Revenue Receivable from Public  | (65)                | (316)              |
| Provision for Losses on Estimated Guaranties  | 4,795               | 8,423              |
| Change in Unfunded Employee Benefits  | 1,136               | 2,112              |
| <b>Total Components Requiring or Generating Resources in Future Periods</b>   | <b>206,743</b>      | <b>373,661</b>     |
| <b>Components Not Requiring or Generating Resources</b>   |                     |                    |
| Depreciation or Amortization  | 2,252               | 459                |
| Change in Bad Debt Expense - Pre-1992 Loans   | (2,057)             | (2,582)            |
| Other (Income) Expenses Not Requiring Budgetary Resources   | (206)               | (7)                |
| <b>Total Components Not Requiring or Generating Resources</b>   | <b>(11)</b>         | <b>(2,130)</b>     |
| <b>Total Components of the Net Cost of Operations that Will Not Require or Generate Resources in the Current Period</b> | <b>206,732</b>      | <b>371,531</b>     |
| <b>Net Cost of Operations</b>   | <b>\$ (466,394)</b> | <b>\$ 524,086</b>  |

Liabilities Not Covered by Budgetary Resources on the Balance Sheet (Note 8) differs from Components Requiring or Generating Resources in Future Periods in this reconciliation primarily due to reestimated subsidy costs of loan programs. The subsidy costs are shown in the Statement of Net Cost and are to be covered by budgetary resources but these resources, while available under permanent and indefinite authority, were not provided by year-end. Additionally, there will always be a difference for existing liabilities because the Reconciliation of Budgetary Obligations Incurred to Net Cost of Operations reports only current year changes, not balances.

The following table details these differences:

(Dollars in Thousands)

| As of September 30,   | 2014              | 2013              |
|---|-------------------|-------------------|
| Current Year Liabilities Not Covered By Budgetary Resources   | \$ 104,408        | \$ 99,012         |
| Less: Prior Year  | 99,012            | 87,637            |
| Change in Liabilities Not Covered By Budgetary Resources  | 5,396             | 11,375            |
| Upward Reestimates of Credit Subsidy Expense  | 200,923           | 362,329           |
| Change in Revenue Receivable from Public  | (65)              | (316)             |
| All Other   | 489               | 273               |
| <b>Components (of Net Cost) Generating Resources in Future Periods<br/>(Per Reconciliation Above)</b> | <b>\$ 206,743</b> | <b>\$ 373,661</b> |

## SUCCESS STORY: Back in Business After Disaster Hits

Pachanga, Inc. d/b/a FIKA, New York, New York

FIKA, which means “coffee break” in Swedish, was the name **Lars Akerlund** gave to each of the five specialty coffee and chocolate cafés he opened in New York beginning in 2006. He was preparing for the New York Chocolate Show in October 2012 when Hurricane Sandy nearly destroyed his Manhattan location and a new place under construction in Tribeca. Flood waters poured into the basement and rose up to four feet on the first floor, destroying all the equipment and thousands of dollars of specially made treats for the chocolate show. Years of hard work were ruined in a matter of minutes, leaving Akerlund with uninsured losses in excess of half a million dollars.

Akerlund received an SBA disaster loan, and with the support of local customers and caring neighbors he started the rebuilding process. In February, he was able to open the new chocolate factory in Tribeca, and two months later the Manhattan location reopened.

Akerlund received the SBA’s *2014 Phoenix Award for Outstanding Small Business Disaster Recovery*. The Phoenix Award is presented to business owners, public officials, and volunteers who display selflessness, ingenuity, and tenacity in the aftermath of a disaster, while contributing to the rebuilding of their communities. “The Phoenix Award acknowledges their heroic efforts and is a symbol of appreciation for their contributions to the economic recovery of their communities,” said SBA Administrator Maria Contreras-Sweet.

“SBA Disaster Assistance saved us,” said Akerlund. “I was so impressed by SBA. Everyone was so incredible.”



# REQUIRED SUPPLEMENTARY INFORMATION

## Combining Statement of Budgetary Resources

For the year ended September 30, 2014 (unaudited)

(Dollars in Thousands)

|  | BLIF              |                           | DLF               |                           | SBGRF             | PCECGF          |
|--|-------------------|---------------------------|-------------------|---------------------------|-------------------|-----------------|
|  | Budgetary         | Nonbudgetary<br>Financing | Budgetary         | Nonbudgetary<br>Financing | Budgetary         | Budgetary       |
| <b>BUDGETARY RESOURCES</b>   |                   |                           |                   |                           |                   |                 |
| Unobligated Balance Brought Forward, October 1   | \$ 198,175        | \$ 3,620,112              | \$ 733,839        | \$ 516,675                | \$ 73,343         | \$ 1,119        |
| Recoveries of Prior Year Obligations   | 29,898            | 3,954                     | 34,815            | 313,144                   | 55                | –               |
| Other Changes in Unobligated Balance   | (19,965)          | (136,244)                 | (3,552)           | (829,550)                 | –                 | (1,119)         |
| Unobligated Balance from Prior Year Budget Authority, net                                  | 208,108           | 3,487,822                 | 765,102           | 269                       | 73,398            | –               |
| Appropriations (discretionary and mandatory)   | 570,219           | –                         | 230,573           | –                         | –                 | –               |
| Borrowing Authority (discretionary and mandatory)  | –                 | 534,107                   | –                 | 228,838                   | –                 | –               |
| Spending Authority from Offsetting Collections   | 17                | 2,668,615                 | 1                 | 882,759                   | 18,624            | –               |
| <b>Total Budgetary Resources</b>   | <b>\$ 778,344</b> | <b>\$ 6,690,544</b>       | <b>\$ 995,676</b> | <b>\$ 1,111,866</b>       | <b>\$ 92,022</b>  | <b>\$ –</b>     |
| <b>STATUS OF BUDGETARY RESOURCES</b>   |                   |                           |                   |                           |                   |                 |
| Obligations Incurred   | \$ 538,257        | \$ 2,825,064              | \$ 257,294        | \$ 628,150                | \$ 11,272         | \$ –            |
| Unobligated Balance, end of year:  |                   |                           |                   |                           |                   |                 |
| Apportioned  | 55,049            | 1,161,522                 | 72,826            | 424,716                   | 19,439            | –               |
| Unapportioned  | 185,038           | 2,703,958                 | 665,556           | 59,000                    | 61,311            | –               |
| Total Unobligated Balance, end of year   | 240,087           | 3,865,480                 | 738,382           | 483,716                   | 80,750            | –               |
| <b>Total Status of Budgetary Resources</b>   | <b>\$ 778,344</b> | <b>\$ 6,690,544</b>       | <b>\$ 995,676</b> | <b>\$ 1,111,866</b>       | <b>\$ 92,022</b>  | <b>\$ –</b>     |
| <b>CHANGE IN OBLIGATED BALANCES</b>  |                   |                           |                   |                           |                   |                 |
| <i>Unpaid Obligations:</i>   |                   |                           |                   |                           |                   |                 |
| Unpaid Obligations, Brought Forward, October 1   | \$ 232,361        | \$ 93,947                 | \$ 67,554         | \$ 607,583                | \$ –              | \$ –            |
| Obligations Incurred   | 538,257           | 2,825,064                 | 257,294           | 628,150                   | 11,272            | –               |
| Gross Outlays  | (611,942)         | (2,827,468)               | (274,985)         | (764,617)                 | (11,188)          | –               |
| Recoveries of Prior Year Unpaid Obligations  | (29,898)          | (3,954)                   | (34,815)          | (313,144)                 | (55)              | –               |
| Unpaid Obligations, end of year  | 128,778           | 87,589                    | 15,048            | 157,972                   | 29                | –               |
| <i>Uncollected Payments:</i>   |                   |                           |                   |                           |                   |                 |
| Uncollected Payments, Federal sources brought forward, October 1                           | –                 | (228,902)                 | –                 | (67,617)                  | –                 | –               |
| Change in Uncollected Payments, Federal Sources  | –                 | 101,021                   | –                 | 52,489                    | –                 | –               |
| Uncollected Payments, Federal Sources, end of year   | –                 | (127,881)                 | –                 | (15,128)                  | –                 | –               |
| <i>Memorandum (non-add) entries:</i>   |                   |                           |                   |                           |                   |                 |
| <b>Obligated Balance, start of year</b>  | <b>\$ 232,361</b> | <b>\$ (134,955)</b>       | <b>\$ 67,554</b>  | <b>\$ 539,966</b>         | <b>\$ –</b>       | <b>\$ –</b>     |
| <b>Obligated Balance, end of year</b>  | <b>\$ 128,778</b> | <b>\$ (40,292)</b>        | <b>\$ 15,048</b>  | <b>\$ 142,844</b>         | <b>\$ 29</b>      | <b>\$ –</b>     |
| <b>BUDGET AUTHORITY AND OUTLAYS, NET</b>   |                   |                           |                   |                           |                   |                 |
| Budget Authority, gross (discretionary and mandatory)                                      | \$ 570,236        | \$ 3,202,722              | \$ 230,574        | \$ 1,111,597              | \$ 18,624         | \$ –            |
| Actual Offsetting Collections (discretionary and mandatory)                                | (8,207)           | (2,872,311)               | (2,183)           | (1,051,247)               | (18,624)          | (425)           |
| Change in Uncollected Customer Payments from Federal Sources (discretionary and mandatory) | –                 | 101,021                   | –                 | 52,489                    | –                 | –               |
| <b>Budget Authority, net (discretionary and mandatory)</b>                                 | <b>\$ 562,029</b> | <b>\$ 431,432</b>         | <b>\$ 228,391</b> | <b>\$ 112,839</b>         | <b>\$ –</b>       | <b>\$ (425)</b> |
| Gross Outlays (discretionary and mandatory)  | \$ 611,942        | \$ 2,827,468              | \$ 274,985        | \$ 764,617                | \$ 11,188         | \$ –            |
| Actual Offsetting Collections (discretionary and mandatory)                                | (8,207)           | (2,872,311)               | (2,183)           | (1,051,247)               | (18,624)          | (425)           |
| Net Outlays (discretionary and mandatory)  | 603,735           | (44,843)                  | 272,802           | (286,630)                 | (7,436)           | (425)           |
| Distributed Offsetting Receipts  | –                 | (1,083,609)               | –                 | (40,446)                  | –                 | –               |
| <b>Agency Outlays, net (discretionary and mandatory)</b>                                   | <b>\$ 603,735</b> | <b>\$ (1,128,452)</b>     | <b>\$ 272,802</b> | <b>\$ (327,076)</b>       | <b>\$ (7,436)</b> | <b>\$ (425)</b> |

See Accompanying Auditors' Report.

## REQUIRED SUPPLEMENTARY INFORMATION (continued)

## Combining Statement of Budgetary Resources

For the year ended September 30, 2014

(Dollars in Thousands)

|  | SE                | OIG              | ADVOCACY        | EDP               | BATF           | TOTAL               | TOTAL                     |                      |
|--|-------------------|------------------|-----------------|-------------------|----------------|---------------------|---------------------------|----------------------|
|  | Budgetary         | Budgetary        | Budgetary       | Budgetary         | Budgetary      | Budgetary           | Nonbudgetary<br>Financing | Total                |
| <b>BUDGETARY RESOURCES</b>   |                   |                  |                 |                   |                |                     |                           |                      |
| Unobligated Balance Brought Forward, October 1   | \$ 280,740        | \$ 9,173         | \$ 679          | \$ –              | \$ 131         | \$ 1,297,199        | \$ 4,136,787              | \$ 5,433,986         |
| Recoveries of Prior Year Obligations   | 40,122            | 134              | 15              | –                 | –              | 105,039             | 317,098                   | 422,137              |
| Other Changes in Unobligated Balance   | (9,195)           | (222)            | –               | –                 | –              | (34,053)            | (965,794)                 | (999,847)            |
| Unobligated Balance from Prior Year Budget Authority, net                                  | 311,667           | 9,085            | 694             | –                 | 131            | 1,368,185           | 3,488,091                 | 4,856,276            |
| Appropriations (discretionary and mandatory)   | 249,500           | 19,000           | 8,750           | 196,665           | –              | 1,274,707           | –                         | 1,274,707            |
| Borrowing Authority (discretionary and mandatory)  | –                 | –                | –               | –                 | –              | –                   | 762,945                   | 762,945              |
| Spending Authority from Offsetting Collections   | 361,672           | 1,001            | 1               | –                 | 41             | 381,357             | 3,551,374                 | 3,932,731            |
| <b>Total Budgetary Resources</b>   | <b>\$ 922,839</b> | <b>\$ 29,086</b> | <b>\$ 9,445</b> | <b>\$ 196,665</b> | <b>\$ 172</b>  | <b>\$ 3,024,249</b> | <b>\$ 7,802,410</b>       | <b>\$ 10,826,659</b> |
| <b>STATUS OF BUDGETARY RESOURCES</b>   |                   |                  |                 |                   |                |                     |                           |                      |
| Obligations Incurred   | \$ 635,606        | \$ 17,854        | \$ 8,628        | \$ 192,274        | \$ 13          | \$ 1,661,198        | \$ 3,453,214              | \$ 5,114,412         |
| Unobligated Balance, end of year:  |                   |                  |                 |                   |                |                     |                           |                      |
| Apportioned  | 236,415           | 9,456            | 817             | 4,391             | 155            | 398,548             | 1,586,238                 | 1,984,786            |
| Unapportioned  | 50,818            | 1,776            | –               | –                 | 4              | 964,503             | 2,762,958                 | 3,727,461            |
| Total Unobligated Balance, end of year   | 287,233           | 11,232           | 817             | 4,391             | 159            | 1,363,051           | 4,349,196                 | 5,712,247            |
| <b>Total Status of Budgetary Resources</b>   | <b>\$ 922,839</b> | <b>\$ 29,086</b> | <b>\$ 9,445</b> | <b>\$ 196,665</b> | <b>\$ 172</b>  | <b>\$ 3,024,249</b> | <b>\$ 7,802,410</b>       | <b>\$ 10,826,659</b> |
| <b>CHANGE IN OBLIGATED BALANCES</b>  |                   |                  |                 |                   |                |                     |                           |                      |
| <i>Unpaid Obligations:</i>   |                   |                  |                 |                   |                |                     |                           |                      |
| Unpaid Obligations, Brought Forward, October 1   | \$ 337,557        | \$ 1,601         | \$ 873          | \$ –              | \$ 5           | \$ 639,951          | \$ 701,530                | \$ 1,341,481         |
| Obligations Incurred   | 635,606           | 17,854           | 8,628           | 192,274           | 13             | 1,661,198           | 3,453,214                 | 5,114,412            |
| Gross Outlays  | (731,508)         | (17,372)         | (8,580)         | (55,323)          | (14)           | (1,710,912)         | (3,592,085)               | (5,302,997)          |
| Recoveries of Prior Year Unpaid Obligations  | (40,122)          | (134)            | (15)            | –                 | –              | (105,039)           | (317,098)                 | (422,137)            |
| Unpaid Obligations, end of year  | 201,533           | 1,949            | 906             | 136,951           | 4              | 485,198             | 245,561                   | 730,759              |
| <i>Uncollected Payments:</i>   |                   |                  |                 |                   |                |                     |                           |                      |
| Uncollected Payments, Federal sources brought forward, October 1                           | –                 | –                | –               | –                 | –              | –                   | (296,519)                 | (296,519)            |
| Change in Uncollected Payments, Federal Sources  | –                 | –                | –               | –                 | –              | –                   | 153,510                   | 153,510              |
| Uncollected Payments, Federal Sources, end of year   | –                 | –                | –               | –                 | –              | –                   | (143,009)                 | (143,009)            |
| <i>Memorandum (non-add) entries:</i>   |                   |                  |                 |                   |                |                     |                           |                      |
| <b>Obligated Balance, start of year</b>  | <b>\$ 337,557</b> | <b>\$ 1,601</b>  | <b>\$ 873</b>   | <b>\$ –</b>       | <b>\$ 5</b>    | <b>\$ 639,951</b>   | <b>\$ 405,011</b>         | <b>\$ 1,044,962</b>  |
| <b>Obligated Balance, end of year</b>  | <b>\$ 201,533</b> | <b>\$ 1,949</b>  | <b>\$ 906</b>   | <b>\$ 136,951</b> | <b>\$ 4</b>    | <b>\$ 485,198</b>   | <b>\$ 102,552</b>         | <b>\$ 587,750</b>    |
| <b>BUDGET AUTHORITY AND OUTLAYS, NET</b>   |                   |                  |                 |                   |                |                     |                           |                      |
| Budget Authority, gross (discretionary and mandatory)                                      | \$ 611,172        | \$ 20,001        | \$ 8,751        | \$ 196,665        | \$ 41          | \$ 1,656,064        | \$ 4,314,319              | \$ 5,970,383         |
| Actual Offsetting Collections (discretionary and mandatory)                                | (361,673)         | (1,001)          | (2)             | –                 | (40)           | (392,155)           | (3,923,558)               | (4,315,713)          |
| Change in Uncollected Customer Payments from Federal Sources (discretionary and mandatory) | –                 | –                | –               | –                 | –              | –                   | 153,510                   | 153,510              |
| <b>Budget Authority, net (discretionary and mandatory)</b>                                 | <b>\$ 249,499</b> | <b>\$ 19,000</b> | <b>\$ 8,749</b> | <b>\$ 196,665</b> | <b>\$ 1</b>    | <b>\$ 1,263,909</b> | <b>\$ 544,271</b>         | <b>\$ 1,808,180</b>  |
| Gross Outlays (discretionary and mandatory)  | \$ 731,508        | \$ 17,372        | \$ 8,580        | \$ 55,323         | \$ 14          | \$ 1,710,912        | \$ 3,592,085              | \$ 5,302,997         |
| Actual Offsetting Collections (discretionary and mandatory)                                | (361,673)         | (1,001)          | (2)             | –                 | (40)           | (392,155)           | (3,923,558)               | (4,315,713)          |
| Net Outlays (discretionary and mandatory)  | 369,835           | 16,371           | 8,578           | 55,323            | (26)           | 1,318,757           | (331,473)                 | 987,284              |
| Distributed Offsetting Receipts  | 900               | –                | –               | –                 | –              | 900                 | (1,124,055)               | (1,123,155)          |
| <b>Agency Outlays, net (discretionary and mandatory)</b>                                   | <b>\$ 370,735</b> | <b>\$ 16,371</b> | <b>\$ 8,578</b> | <b>\$ 55,323</b>  | <b>\$ (26)</b> | <b>\$ 1,319,657</b> | <b>\$ (1,455,528)</b>     | <b>\$ (135,871)</b>  |

## REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION

(Unaudited)

### Stewardship Investments in Human Capital

Human Capital investments are expenses included in net cost for education and training programs that are intended to increase or maintain national economic productive capacity and that produce outputs and outcomes that provide evidence of maintaining or increasing national productive capacity. The definition excludes education and training expenses for federal personnel.

**Small Business Development Centers** deliver an array of services to small businesses and prospective business owners using an extensive network of lead centers and outreach locations. SBDCs deliver professional business advice and training assistance in key management areas to small business clients throughout the U.S. that generates business revenue, creates and retains jobs, and enhances local and regional economies.

**SCORE** is a nonprofit association comprised of over 11,000 volunteer mentors and business advice counselors that serve entrepreneurs with in-person mentoring, local training workshops, and online resources. SCORE adapts its structure and services to meet the needs of specific small businesses.

**Women's Business Centers** provide business advice and training assistance primarily to women entrepreneurs through over 100 non-profit educational centers across the nation. Many of the training courses focus on business and financial planning that help women entrepreneurs gain financial literacy. They also provide direct business advice to clients and help them access loans, federal contracts, and exporting opportunities.

**Microloan Technical Assistance** helps the smallest of small businesses become established and achieve success. Community-based intermediary lenders provide business-based training and technical assistance to microbusinesses. The program is an important source of training assistance for low-income, women, veteran, and minority entrepreneurs.

**SBA's Consulting and Training Programs** includes SBA's work to develop or expand business advice and training assistance programs focused on key areas, including underserved markets, procurement, exports, and emerging and expanding technological sectors. These small business counseling and training programs are provided by or facilitated through an SBA district office for the delivery of a structured program providing knowledge, information or experience on a business-related subject. Training is available on a number of subjects of interest to a small business person and may be delivered to an individual, a class, or online.

**Veterans Outreach** includes comprehensive outreach through veterans business outreach centers and technical assistance and training to transitioning veterans that are interested in starting a new or growing an existing business through programs such as Boots-to-Business, Veteran Women Igniting the Spirit of Entrepreneurship, and Entrepreneurship Boot Camp for Veterans with Disabilities.

**All Other Training and Assistance Programs** not separately detailed include PRIME Technical Assistance, Native American Outreach and the 7(j) program.

Performance results are provided in the Management's Discussion and Analysis section of SBA's Agency Financial Report in "SBA by the Numbers" and "Summary of Key SBA Programs".

Significant Human Capital investments occur within the following programs:

(Dollars in Thousands)

| For the Five Years Ended September 30,     | 2014              | 2013              | 2012              | 2011              | 2010              |
|--|-------------------|-------------------|-------------------|-------------------|-------------------|
| Small Business Development Centers         | \$ 154,400        | \$ 93,427         | \$ 152,835        | \$ 123,097        | \$ 130,046        |
| SCORE                                      | 5,758             | 10,894            | 9,331             | 14,094            | 11,134            |
| Women's Business Centers                   | 24,842            | 21,049            | 25,006            | 13,080            | 16,924            |
| Microloan Technical Assistance             | 21,552            | 16,525            | 22,487            | 30,485            | 23,426            |
| SBA's Consulting and Training Programs     | 54,620            | 44,313            | 28,365            | 28,006            | 20,576            |
| Veterans Outreach                          | 13,244            | —                 | —                 | —                 | —                 |
| All Other Training and Assistance Programs | 12,832            | 6,924             | 12,689            | 8,603             | 37,055            |
| <b>Total</b>                               | <b>\$ 287,248</b> | <b>\$ 193,132</b> | <b>\$ 250,713</b> | <b>\$ 217,365</b> | <b>\$ 239,161</b> |

Note: FY 2013 amounts above differ from the published year-end FY 2013 amounts due to the change in the net cost allocations (see Note 14).