

# Rules and Regulations

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This section of the FEDERAL REGISTER contains regulatory documents having general applicability and legal effect, most of which are keyed to and codified in the Code of Federal Regulations, which is published under 50 titles pursuant to 44 U.S.C. 1510.

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## DEPARTMENT OF AGRICULTURE

### Rural Utilities Service

#### 7 CFR Part 1773

RIN 0572-AC33

#### Policy on Audits of RUS Borrowers and Grantees

**AGENCY:** Rural Utilities Service, USDA.

**ACTION:** Final rule with request for comment.

**SUMMARY:** The Rural Utilities Service (RUS) is amending its regulations regarding its Policy on Audits to incorporate 2011 revisions to the Generally Accepted Government Auditing Standards (GAGAS) issued by the Government Accountability Office (GAO), the clarified audit standards issued by the American Institute of Certified Public Accountants (AICPA) in 2011, and Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, Subpart F, Audit Requirements, issued by the Office of Management and Budget on December 26, 2013, and adopted by USDA on December 26, 2014. RUS is also expanding and clarifying its regulations to: include grant recipients, amend its peer review requirements, amend its reporting requirements, expand the options for the electronic filing of audits, and clarify a number of existing audit requirements, and is amending the title to reflect this change.

**DATES:** *Effective Date:* Rule will become effective on July 6, 2018 and is applicable for financial audits for periods ending on or after December 15, 2018.

*Comment Date:* Comments must be received by RUS on or before June 6, 2018.

**ADDRESSES:** Submit comments by either of the following methods:

- Federal eRulemaking Portal at <https://www.regulations.gov/>. Follow instructions for submitting comments.

- *Postal Mail/Commercial Delivery:*

Please send your comments addressed to Thomas P. Dickson, Acting Director, Program Development and Regulatory Analysis, Rural Utilities Service, U.S. Department of Agriculture, 1400 Independence Avenue SW, STOP 1522, Room 5164-S, Washington, DC 20250-1522.

Additional information about Rural Development and its programs is available on the internet at <https://www.rd.usda.gov/>.

#### FOR FURTHER INFORMATION CONTACT:

William Chris Colberg, Acting Chief, Technical Accounting and Auditing Staff, Program Accounting Services Division, Rural Utilities Service, U.S. Department of Agriculture, 1400 Independence Avenue SW, STOP 1523, Washington, DC 20250-1523. Telephone: (202) 720-1905.

#### SUPPLEMENTARY INFORMATION:

##### Executive Order 12866

This final rule has been determined to be not significant for the purposes of Executive Order 12866 and, therefore, has not been reviewed by the Office of Management and Budget (OMB).

##### Executive Order 12372

This final rule is excluded from the scope of Executive Order 12372, Intergovernmental Consultation, which may require consultation with state and local officials. See the final rule related notice entitled, "Department Programs and Activities Excluded from Executive Order 12372" (50 FR 47034) advising that RUS loans and loan guarantees were not covered by Executive Order 12372.

##### Executive Order 12988

This final rule has been reviewed under Executive Order 12988, Civil Justice Reform. RUS has determined that this final rule meets the applicable standards provided in section 3 of the Executive Order. In addition, all state and local laws and regulations that are in conflict with this rule will be preempted, no retroactive effect will be given to this rule, and, in accordance with section 212(e) of the Department of Agriculture Reorganization Act of 1994 (7 U.S.C. 6912(e)), administrative appeal procedures, if any, must be exhausted before an action against the Department or its agencies may be initiated.

### Regulatory Flexibility Act Certification

RUS has determined that this final rule will not have significant impact on a substantial number of small entities defined in the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*). The RUS loan programs provide borrowers with loans at interest rates and terms that are more favorable than those generally available from the private sector. Borrowers, as a result of obtaining federal financing, receive economic benefits that exceed any direct cost associated with RUS regulations and requirements.

### National Environmental Policy Act Certification

RUS has determined that this final rule will not significantly affect the quality of the human environment as defined by the National Environmental Policy Act of 1969 (42 U.S.C. 4321 *et seq.*). Therefore, this action does not require an environmental impact statement or assessment.

### Catalog of Federal Domestic Assistance

The programs described by this final rule are listed in the Catalog of Federal Domestic Assistance under Numbers CFDA 10.751, Rural Energy Savings Program; CFDA 10.787, Broadband Initiatives Program; CFDA 10.850, Rural Electrification Loans and Loan Guarantees; CFDA 10.851, Rural Telephone Loans and Loan Guarantees; CFDA 10.855, Distance Learning and Telemedicine Loans and Grants; CFDA 10.857, Bulk Fuel Revolving Fund Grants; CFDA 10.858, Denali Commission Grants and Loans; CFDA 10.859, Assistance to High Energy Cost Rural Communities; CFDA 10.861, Public Television Station Digital Transition Grant Program; and, CFDA 10.863, Community Connect Grant Program. The General Services Administration (GSA) website at <http://www.cfda.gov> contains a PDF file version of the CFDA catalog. The print edition of the catalog may be purchased from the U.S. Government Publishing Office (GPO) by calling (202) 512-1800 or toll free at 1-866-512-1800, or by ordering it online at <http://bookstore.gpo.gov>.

### Information Collection and Recordkeeping Requirements

The reporting and recordkeeping requirements contained in this final rule have been approved by the Office of

Management and Budget (OMB) under OMB Control Number 0572–0095, pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C Chapter 35). This final rule contains no new reporting or recordkeeping burdens under OMB Control Number 0572–0095 that would require approval under the Paperwork Reduction Act.

Send questions or comments regarding this burden or any other aspect of these collections of information, including suggestions for reducing the burden, to Thomas P. Dickson, Acting Director, Program Development and Regulatory Analysis, Rural Utilities Service, U.S. Department of Agriculture, 1400 Independence Avenue SW, Stop 1522, Room 5164–S, Washington, DC 20250–1522.

#### Unfunded Mandates

This final rule contains no Federal mandates (under the regulatory provision of title II of the Unfunded Mandates Reform Act of 1995) for state, local, and tribal governments or the private sector. Thus, this final rule is not subject to the requirements of sections 202 and 205 of the Unfunded Mandates Reform Act of 1995.

#### Comments

We invite you to participate in this rulemaking by submitting written comments, data, or views before the noted deadline. We will consider the comments we received and may conduct additional rulemaking based on the comments.

#### Background

7 CFR part 1773, Policy on Audits of RUS Borrowers and Grantees (Part 1773), implements the standard RUS security instrument provision requiring RUS electric and telecommunications borrowers and grantees to prepare and furnish to RUS, at least once during each 12-month period, a full and complete report of its financial condition, operations, and cash flows, in form and substance satisfactory to RUS; audited and certified by an independent audit organization, satisfactory to RUS, and accompanied by a report of such audit, in form and substance satisfactory to RUS. This rule is amended to include coverage of all grantees and the title of Part 1773 is revised to reflect this change.

This rule amends Part 1773 to incorporate the 2011 revisions to GAGAS by the GAO issued in December 2011. The 2011 revision contains major changes that reinforce the principles of transparency and accountability and provide the framework for high-quality government audits that add value. This

revision to GAGAS incorporates the AICPA Statements on Auditing Standards. The 2011 revisions to GAGAS were effective for financial audits for periods ending on or after December 15, 2012.

The professional standards and guidance contained in GAGAS provide a framework for conducting high quality audits with competence, integrity, objectivity, and independence. These standards are used by auditors of entities that receive government awards and audit organizations performing GAGAS audits. GAGAS contains standards for audits as well as requirements and guidance dealing with ethics, independence, auditors' professional judgment and competence, quality control, performance of the audit, and reporting.

This rule amends Part 1773 to incorporate the clarified audit standards issued by the AICPA in October 2011. The purpose of redrafting the auditing standards was for clarity and convergence although there were some changes and additions in terms of requirements. The clarified standards also introduced new terminology and new audit reports by adding extra paragraphs and segregating sections of the report under subheadings.

In 2013, the Office of Management and Budget (OMB) revised uniform administrative requirements, cost principles, and audit requirements for Federal awards by issuing 2 CFR part 200, which served to consolidate and replace OMB Circulars A–21, A–87, A–89, A–102, A–110, A–122, and A–133. 2 CFR part 200 was adopted by USDA in December 2014. The portion of this CFR applicable to audits, Subpart F, is recognized and adopted by this revision to Part 1773.

This rule revises all subparts to encompass grantees, to remove most references to Rural Telephone Bank (RTB), to conform the language used to generally accepted auditing standards (GAAS) issued by the AICPA and GAGAS. This rule adds, changes or deletes definitions as appropriate to clarify certain existing information. Perhaps most importantly, this rule replaces the RUS management letter with a report on compliance with aspects of contractual agreements and regulatory requirements based on the requirements found in AU–C 806 of GAAS. This rule also provides information on the electronic filing of annual audits in § 1773.21. RUS is also adding a requirement to the reporting package for a schedule of findings and recommendations in § 1773.34.

Due to the state boards of accountancy having now adopted peer review

requirements as part of the CPA licensing requirements for performing attestation services, this amended rule significantly streamlines the RUS peer review monitoring included in § 1773.5 by removing much of the guidance previously provided with regard to auditor participation in an approved peer review program. RUS will no longer require that all auditors submit copies of their peer review reports but reserves the right to request said reports on a case by case basis. It also removes the option of requesting a waiver of the peer review requirement, relying instead on the requirements of the state boards of accountancy and the guidance provided within the peer review programs themselves.

Due to the scope and pervasiveness of the revisions being implemented, Part 1773 as revised is being published in its entirety in this final rule.

In this revision to Part 1773, all sample reports and financial statements will be combined into four appendices which will be available in RUS Bulletin 1773–1, Policy on Audits of RUS Borrowers and Grantees. Appendix A of RUS Bulletin 1773–1 contains the sample reports, financial statements and schedule of findings and recommendations for electric borrowers; Appendix B contains similar samples for telecommunications borrowers; Appendix C for broadband borrowers; and Appendix D contains sample reports for grantees. Appendices A through D will not be printed in the Code of Federal Regulations; however, these appendices are available at <https://www.regulations.gov/> for review and comment in conjunction with the comment period for this final rule. Only Subparts A through E will be published in the Code of Federal Regulations. The appendices are included in RUS Bulletin 1773–1, Policy on Audits of RUS Borrowers and Grantees, which contains all of Part 1773, including subparts A through E and the appendices. Publishing Part 1773 in bulletin form provides the RUS audit policy in an easy to read format. This publication is available on RUS' website at <https://www.rd.usda.gov/publications/regulations-guidelines/rural-utilities-service-audit>.

#### USDA Non-Discrimination Statement

In accordance with Federal civil rights law and U.S. Department of Agriculture (USDA) civil rights regulations and policies, the USDA, its Agencies, offices, and employees, and institutions participating in or administering USDA programs are prohibited from discriminating based on race, color, national origin, religion, sex,

gender identity (including gender expression), sexual orientation, disability, age, marital status, family/parental status, income derived from public assistance programs, political beliefs, or reprisal or retaliation for prior civil rights activity, in any program or activity conducted or funded by USDA (not all bases apply to all programs). Remedies and complaint filing deadlines vary by program or incident.

Persons with disabilities who require alternative means of communication for program information (e.g., Braille, large print, audiotape, American Sign Language, etc.) should contact the responsible Agency or USDA's TARGET Center at (202) 720-2600 (voice and TTY) or contact USDA through the Federal Relay Service at (800) 877-8339. Additionally, program information may be made available in languages other than English.

To file a program discrimination complaint, complete the USDA Program Discrimination Complaint Form, AD-3027, found online at <https://www.ascr.usda.gov/filing-program-discrimination-complaint-usda-customer> and at any USDA office or write a letter addressed to USDA and provide in the letter all of the information requested in the form. To request a copy of the complaint form, call (866) 632-9992. Submit your completed form or letter to USDA by:

(1) *Mail*: U.S. Department of Agriculture, Office of the Assistant Secretary for Civil Rights, 1400 Independence Avenue SW, Washington, DC 20250-9410;

(2) *fax*: (202) 690-7442; or

(3) *email*: [program.intake@usda.gov](mailto:program.intake@usda.gov).

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#### List of Subjects in 7 CFR Part 1773

Accounting, Auditing, Electric power, Grants, Loan programs—broadband, Loan programs—communications, Loan programs—energy, Reporting and recordkeeping requirements, Rural areas, Telephone.

■ For the reasons set forth in the preamble, RUS revises 7 CFR part 1773 to read as follows:

### PART 1773—POLICY ON AUDITS OF RUS BORROWERS AND GRANTEEES

#### Subpart A—General Provisions

Sec.

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1773.2 Definitions.

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1773.8 Audit date.

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1773.10 Access to audit documentation.

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#### Subpart C—RUS Requirements for the Submission and Review of the Reporting Package

1773.20 The auditor's submission of the reporting package.

1773.21 Auditee's review and submission of the reporting package.

1773.22–1773.29 [Reserved]

#### Subpart D—RUS Reporting Requirements

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1773.31 Auditor's report on the financial statements.

1773.32 Report on internal control over financial reporting and on compliance and other matters.

1773.33 Report on compliance with aspects of contractual agreements and regulatory requirements.

1773.34 Schedule of findings and recommendations.

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#### Subpart E—RUS Audit Requirements and Documentation

1773.38 Scope of engagement.

1773.39 Utility plant and accumulated depreciation.

1773.40 Regulatory assets.

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1773.43 Capital and equity accounts.

1773.44 Long-term debt.

1773.45 Regulatory liabilities.

1773.46–1773.48 [Reserved]

1773.49 OMB Control Number.

**Authority:** 7 U.S.C. 901 *et seq.*, 7 U.S.C. 1921 *et seq.*, 7 U.S.C. 6941 *et seq.*

#### Subpart A—General Provisions

##### § 1773.1 General.

(a) This part implements the standards for audits required by the loan and grant agreements of Rural Utilities Service (RUS) electric and telecommunications borrowers and grantees. The provisions require auditees to prepare and furnish to RUS, at least once during each 12-month period, a full and complete report of its financial condition, operations, and cash flows, in form and substance satisfactory to RUS, audited and certified by an independent auditor, satisfactory to RUS, and accompanied by a report of such audit, in form and substance satisfactory to RUS.

(b) This part is based on the requirements of GAGAS in effect at the time of the audit and applicable RUS regulations and subpart F (Audit Requirements) of 2 CFR part 200 (Uniform Administrative Requirements, Cost Principles, and Audit

Requirements for Federal Awards) (2 CFR 200.500–200.521).

(c) This part further sets forth the criteria for selecting auditors satisfactory to RUS and certain audit procedures and audit documentation that must be performed and prepared before an audit report will be accepted by RUS.

(d) Failure to provide an audit in compliance with this part is a serious violation of the RUS Security Agreement. RUS relies on audited financial statements in order to assess and monitor the financial condition of its borrowers and grantees and to fulfill its fiduciary responsibilities.

(e) RUS reserves the right to suspend its acceptance of audits performed by auditors who, in the opinion of RUS, are not meeting the requirements of this part or with unresolved disputes or issues until such time that the matter can be resolved to RUS' satisfaction.

#### § 1773.2 Definitions.

As used in this part:

*2 CFR part 200, subpart F* means 2 CFR part 200, Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards, subpart F, Audit Requirements, as adopted by USDA in 2 CFR part 400.

*AA-PARA* means RUS Assistant Administrator, Program Accounting and Regulatory Analysis.

*Administrator* means the Administrator of RUS.

*Affiliated company* means a company that directly or indirectly through one or more intermediaries, control or are controlled by, or are under common control with, the auditee.

*AICPA* means the American Institute of Certified Public Accountants.

*ASC* means the Accounting Standards Codification issued by the Financial Accounting Standards Board.

*Audit* means an examination of financial statements by an independent auditor for the purpose of expressing an opinion on the fairness with which those statements present financial position, results of operations, and changes in cash flows in accordance with accounting principles generally accepted in the United States of America (GAAP) and for determining whether the auditee has complied with applicable laws, regulations, and provisions of loan or grant contracts and grant agreements that could have a material effect on the financial statements.

*Audit date* means the “as of” date established by the auditee.

*Audit documentation* has the same meaning as defined in the AICPA's professional auditing standards.

*Auditee* means an RUS borrower and/or grantee that is required to submit an annual audit as a condition of the award.

*Auditor* means government auditors as well as certified public accounting firms that perform audits using generally accepted government auditing standards (GAGAS).

*BCAS* means Broadband Collection and Analysis System (or successor system).

*Borrower* means an entity that has an outstanding RUS or Federal Financing Bank (FFB) loan or loan guarantee.

*CPA* means a Certified Public Accountant.

*DCS* means the Data Collection System (or successor system).

*FASB* means Financial Accounting Standards Board.

*FFB* means the Federal Financing Bank, a body corporate and instrumentality of the United States of America under the general supervision of the Secretary of the Department of the Treasury.

*Fraud* has the same meaning as defined in the AICPA's professional auditing standards.

*GAAP* has the same meaning as defined in accounting standards issued by the Government Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB).

*GAGAS* means generally accepted government auditing standards as set forth in Government Auditing Standards, issued by the Comptroller General of the United States, Government Accountability Office.

*GAO* means the United States Government Accountability Office.

*GASB* means Government Accounting Standards Board.

*Governance board* means the auditee's board of directors, managing members, or other official body charged with governance.

*Grantee* means an entity that has a continuing responsibility under a grant agreement with RUS.

*Illegal act* has the same meaning as defined by the Public Company Accounting Oversight Board.

*Material weakness* has the same meaning as defined in the AICPA's professional auditing standards.

*OIG* means the Office of the Inspector General, United States Department of Agriculture.

*OMB* means The Office of Management and Budget.

*Regulatory asset* means an asset resulting from an action of a regulator as defined by FASB.

*Regulatory liability* means a liability imposed on a regulated enterprise by an

action of a regulator as defined by FASB.

*Related party* has the same meaning as defined by FASB.

*Reporting package* means:

(1) The auditor's report on the financial statements;

(2) The report on internal control over financial reporting and on compliance and other matters;

(3) The report on compliance with aspects of contractual agreements and regulatory requirements;

(4) The schedule of findings and recommendations; and

(5) All supplemental schedules and information required by this part.

*RUS* means the Rural Utilities Service, an agency of the United States Department of Agriculture.

*RUS Bulletin 1773-1*, Policy on Audits of RUS Borrowers and Grantees, is a publication prepared by RUS that contains the RUS regulation 7 CFR part 1773 and exhibits of sample audit reports, financial statements, reports on internal control over financial reporting and on compliance and other matters, report on compliance with aspects of contractual agreements and regulatory requirements, and schedule of findings and recommendations used in preparing audits of RUS borrowers and grantees. This bulletin is available on the internet at <https://www.rd.usda.gov/publications/regulations-guidelines/bulletins/program-accounting>.

*RUS security agreement* means a loan agreement, grant agreement, mortgage, security agreement, or other form of agreement that governs the terms and conditions of, or provides security for, loan and/or grant funds provided by RUS to the auditee.

*Significant deficiency* has the same meaning as defined in the AICPA's professional auditing standards.

*Single Audit Act* means Single Audit Act of 1984 (31 U.S.C. 7501 *et seq.*) as implemented by 2 CFR part 200, subpart F.

*State* means any state or territory of the United States, or the District of Columbia.

*Uniform System of Accounts* means, for telecommunications borrowers, Bulletin 1770B-1, Accounting Requirements for RUS Telecommunications Borrowers ([https://www.rd.usda.gov/files/UTP\\_Bulletins\\_1770B-1.pdf](https://www.rd.usda.gov/files/UTP_Bulletins_1770B-1.pdf)), and for electric borrowers, as contained in 7 CFR part 1767, Accounting Requirements for RUS Electric Borrowers, subpart B—Uniform System of Accounts, Bulletin 1767B-1, ([https://www.rd.usda.gov/files/UPA\\_Bulletin\\_1767B-1.pdf](https://www.rd.usda.gov/files/UPA_Bulletin_1767B-1.pdf)).

## Subpart B—RUS Audit Requirements

### § 1773.3 Annual audit.

(a) Each auditee must have its financial statements audited annually by an auditor selected by the auditee and approved by RUS as set forth in § 1773.4. All auditees must submit audited financial statements on a comparative basis covering two consecutive 12 month periods, unless the entity has not been in existence for two consecutive 12-month audit periods. Consolidated statements of the parent are not an acceptable replacement for an audit of the auditee.

(b) Each auditee must establish an annual audit date within 12 months of the date of the first advance and must prepare annual financial statements for the audit date established. Each auditee must notify the AA-PARA of the audit date at least 90 days prior to the selected audit date.

(c) Auditees must furnish a reporting package to RUS within 120 days of the audit date. (See § 1773.21). Until all loans made or guaranteed by RUS are repaid and unliquidated obligations rescinded, auditees that are borrowers must continue to provide annual audited financial statements. Auditees that are grantees must furnish annual audited financial statements in the year of the first advance and until all funds have been advanced or rescinded, and all financial compliance requirements have been fully satisfied.

(d) In addition to the requirements of this part, certain auditees may be subject to the Single Audit Act. An auditee that is defined as a Non-Federal Entity as defined in 2 CFR 200.69 means a state, local government, Indian tribe, institution of higher education (IHE), or nonprofit organization that carries out a Federal award as a recipient or subrecipient and is required to meet the requirements of this part as follows:

(1) Borrowers and/or grantees expending the threshold established for the Single Audit Act (currently \$750,000) or more in Federal awards during the year must have an audit performed in accordance with the Single Audit Act. See 2 CFR 200.502, Basis For Determining Federal Awards Expended, for guidance in determining annual expenditures. The audited financial statements must be submitted to RUS and to the Federal Audit Clearinghouse.

(2) For auditees expending less than the threshold for expenditure in Federal awards during the year, RUS reserves its right under 2 CFR 200.503, Relationship to other audit requirements, to arrange for an audit performed in accordance with this part.

(3) Within 30 days of the audit date, auditees must notify the AA-PARA, in writing, of the total Federal awards expended during the year and must state whether the audit will be performed in accordance with the Single Audit Act, or this part.

(i) An auditee electing to comply with this part must select an auditor that meets the qualifications set forth in § 1773.5.

(ii) If an audit is performed in accordance with the Single Audit Act, the auditor's reporting on the financial statements that meet the requirements of the Single Audit Act, will be sufficient to satisfy the auditee's obligations under this part.

(e) Subpart F of 2 CFR part 200 does not apply to audits of RUS electric and telecommunications cooperatives and for-profit telecommunications borrowers unless the borrower has contractually agreed with another Federal agency (e.g. Federal Emergency Management Agency) to provide a financial audit performed in accordance with 2 CFR part 200, subpart F. In no circumstance will an auditee be required to submit separate audits performed in accordance with this part and 2 CFR part 200, subpart F.

#### § 1773.4 Auditee's responsibilities.

(a) *Selection of a qualified auditor.* The auditee's governance board is responsible for the selection of a qualified auditor that meets the requirements set forth in § 1773.5. When selecting an auditor, the auditee should consider, among other matters:

(1) The qualifications of auditors available to do the work;

(2) The auditor's experience in performing audits of utilities, related industries, or in the case of grantees, experience in auditing entities comparable to the grantee; and

(3) The auditor's ability to complete the audit and submit the reporting package within 90 days of the audit date.

(b) *Board approval of selection.* The board's approval of an auditor must be recorded by a board resolution that states:

(1) The auditor represents that it meets RUS qualifications to perform an audit; and

(2) The auditee and auditor will enter into an audit engagement in accordance with § 1773.6.

(c) *Notification of selection.* When the initial selection or subsequent change of an auditor has been made, the auditee must notify the AA-PARA, in writing, at least 90 days prior to the audit date.

(1) Within 30 days of the date of receipt of such notice, RUS will notify

the auditee, in writing, if the selection or change in auditor is not satisfactory.

(2) Notification to RUS that the same auditor has been selected for succeeding audits of the auditee's financial statements is not required; however, the procedures outlined in this part must be followed for each new auditor selected, even though such auditor may previously have been approved by RUS to audit records of other RUS auditees. Changes in the name of an auditor are considered to be a change in the auditor.

(d) *Audit engagement letter.* The auditee must enter into an audit agreement with the auditor that complies with § 1773.6 prior to the initiation of the audit.

(e) *Debarment certification.* The auditee must obtain, from the selected auditor, a lower tier covered transaction certification (Form AD-1048, Certification Regarding Debarment, Suspension, Ineligibility and Voluntary Exclusion—Lower Tier Covered Transactions), as required by Executive Orders 12549 and 12689, Debarment and Suspension, and any rules or regulations issued thereunder.

(f) *Peer review report.* The auditee must obtain, from the selected auditor, a copy of the auditor's current approved peer review report.

(g) *Preparation of schedules.* The auditee must prepare any schedules that are required by the auditor to perform the audit, including a schedule of deferred debits and deferred credits and a detailed schedule of investments in subsidiary and affiliated companies accounted for on the cost, equity, or consolidated basis. The detailed schedule of investments can be included in the notes to the financial statements or as a separate schedule as long as all information required is adequately disclosed. Samples of these schedules can be found in Appendices A-D, of RUS Bulletin 1773-1.

(1) The schedule of deferred debits and deferred credits must include a description of the deferral and a notation as to whether the deferral has received written approval from RUS. If a determination is made that prior written approval is not required, cite the specific authority for the deferral.

(2) The schedule of investments must include investments in subsidiary and affiliated companies, corporations, limited liability corporations and partnerships, joint ventures, etc.

accounted for on either the cost, equity or on a consolidated basis. For all investments, the auditee must list the name of the entity, ownership percentage, and the principal business in which the entity is engaged. For investments recorded on the cost basis,

the auditee must include the original investment, advances, dividends declared or paid in the current and prior years and the net investment. For investments recorded on the equity or consolidated basis, the auditee must include the ownership percentage, original investment, advances, dividends declared or paid in the current and prior years, and current and prior years' earnings and losses, including accumulated losses in excess of the original investment.

(h) *Scope limitations.* The auditee will not limit the scope of the audit to the extent that the auditor is unable to provide an unqualified opinion that the financial statements are presented fairly in conformity with GAAP due to the scope limitation.

(i) *Submission of reporting package.* The auditee must submit to RUS the required reporting package as set forth in § 1773.21.

(1) A reporting package that fails to meet the requirements detailed in this part will be returned to the auditee with a written explanation of noncompliance.

(2) The auditee must, within 30 days of the date of the letter or email detailing the noncompliance, submit a corrected reporting package to RUS.

(3) If a corrected reporting package is not received within 30 days of the date of the letter or email detailing the noncompliance, RUS will take appropriate action, depending on the severity of the noncompliance.

(j) *Submission of a plan of corrective action.* If the auditor's report contains findings and recommendations but does not include the auditee's response, the auditee must submit written responses to RUS within 180 days of the audit date. The written responses must address:

(1) The corrective action already taken or planned, or the reason the auditee believes no action is necessary; and

(2) The status of corrective action taken on previously reported findings and recommendations.

#### § 1773.5 Qualifications of the auditor.

Auditors that meet the qualifications criteria of this section and enter into an audit engagement with the auditee that complies with § 1773.6, will be considered satisfactory to RUS.

(a) *Licensing.* Auditors that audit the financial statements of an RUS auditee must be licensed to perform attestation engagements in the United States of America. Auditors do not have to be licensed by the state in which the auditee is located; however, auditors must abide by the rules and regulations of professional conduct promulgated by

the accountancy board of the state in which the auditee is located.

(b) *Independence.* Auditors must be independent as determined by the standards for independence in the AICPA Code of Professional Conduct and in GAGAS in effect at the time of the audit.

(c) *Peer review requirement.* Auditors must be enrolled and participating in a peer review program, and must have undergone a satisfactory peer review of their accounting and audit practice. The peer review must be in effect at the date of the audit report opinion.

(1) *Peer review reports.* RUS reserves the right to request peer review reports from selected auditors.

(2) *Peer review requirements for new auditors.* New auditing firms must meet the requirements of their state board of accountancy with regard to enrolling in a peer review program, timing of the first peer review, and any other peer review requirements.

#### **§ 1773.6 Auditor communication.**

(a) GAGAS and AICPA standards require that the auditor communicate with the auditee the auditor's understanding of the services to be performed and document that understanding through a written communication to those charged with governance. To be acceptable to RUS, the auditor's communication must take the form of an audit engagement letter prepared by the auditor and must be formally accepted by the governance board or an audit committee representing the governance board. In addition to the requirements of the AICPA's professional auditing standards and GAGAS, the engagement letter must also include the following:

(1) The nature of planned work and level of assurance to be provided related to internal control over financial reporting and compliance with laws, regulation, and provision of contracts or grant agreements;

(2) That the auditee and auditor acknowledge that the audit is being performed and that the reporting package is being issued to enable the auditee to comply with the provisions of RUS's security instrument which requires compliance with this part;

(3) That the auditor acknowledges the mandatory reporting requirements for fraud, illegal acts, or noncompliance with provisions of laws, regulations, contracts, and grant agreements in § 1773.9. Acceptance of the engagement letter by the auditee is required, thus granting the auditor permission to directly notify the appropriate officials which may include but is not limited to the governance board, RUS, and OIG;

(4) That the auditor acknowledges that it is required under § 1773.7 to contact RUS if the auditor is unable to resolve scope limitations imposed by the auditee, or if such limitations in scope violate this part. Acceptance of the engagement letter by the auditee is required, thus granting the auditor permission to directly notify the AA-PARA as needed;

(5) That the auditee and auditor acknowledge that RUS will consider the auditee to be in violation of its RUS Security Agreement and this part if the auditee fails to have an audit performed and documented in compliance with GAGAS and this part;

(6) That the auditor represents that it meets the requirements under this part to perform the audit;

(7) That the auditor will perform the audit and will prepare the reporting package in accordance with the requirements of this part;

(8) That the auditor will document the audit work performed in accordance with GAGAS, and the requirements of this part; and

(9) That the auditor will make all audit documentation, including the reporting package available to RUS or its representatives (including but not limited to OIG and GAO), upon request, and will permit the photocopying of all such audit documentation.

(b) A copy of the audit engagement letter must be available at the auditee's office for inspection by RUS personnel. One copy of the current audit engagement letter must be maintained in the auditor's audit documentation.

#### **§ 1773.7 Audit standards.**

(a) The audit of the financial statements must be performed in accordance with GAGAS and this part in effect at the audit date unless the auditee is directed otherwise, in writing, by RUS.

(b) The audit of the financial statements must include such tests of the accounting records and such other auditing procedures that are sufficient to enable the auditor to express an opinion on the financial statements and to issue the required reporting package.

(c)(1) The auditee will not limit the scope of the audit to the extent that the auditor is unable to meet RUS audit requirements without prior written approval of the AA-PARA.

(2) If the auditor determines during the audit that an unqualified opinion cannot be issued due to a scope limitation imposed by the auditee, the auditor should use professional judgment to determine what levels of the auditee's management and/or those

charged with governance should be informed.

(3) After informing the auditee's management and/or those charged with governance, if the scope limitation is not adequately resolved, the auditor should immediately contact the AA-PARA.

#### **§ 1773.8 Audit date.**

(a) The annual audit must be performed as of the end of the same calendar month each year unless prior approval to change the audit date is obtained, in writing, from RUS.

(1) An auditee may request a change in the audit date by writing to the AA-PARA at least 60 days prior to the currently approved audit date, providing justification for the change.

(2) The time period between the prior audit date and the newly requested audit date must be no longer than twenty-three months.

(3) Comparative financial statements must be prepared and audited for the 12 months ending as of the new audit date and for the 12 months immediately preceding that period.

#### **§ 1773.9 Disclosure of fraud, and noncompliance with provisions of laws, regulations, contracts, and loan and grant agreements.**

(a) In accordance with GAGAS, the auditor is responsible for planning and performing the audit to provide reasonable assurance about whether the financial statements are free of material misstatement due to error or fraud. The auditor must also plan the audit to provide reasonable assurance of detecting material misstatements resulting from violations of provisions of laws, regulations, contracts or loan and grant agreements that could have a direct and material effect on the financial statements.

(b) If specific information comes to the auditor's attention that provides evidence concerning the existence of possible violations of provisions of laws, regulations, contracts or loan and grant agreements that could have a material indirect effect on the financial statements, the auditor should apply audit procedures specifically directed to ascertaining whether a violation of provisions of laws, regulations, contract or grant agreements has occurred.

(c) Pursuant to the terms of its audit engagement letter with the auditee, the auditor must immediately report, in writing, all instances of fraud, illegal acts, and all indications or instances of noncompliance with laws, whether material or not, to:

(1) The president of the auditee's governance board;

(2) AA-PARA; and

(3) OIG, as follows:

(i) For all audits performed in accordance with § 1773.3(d) (audits conducted in accordance with 2 CFR part 200 “Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards”), report to the USDA-OIG-Audit, National Single Audit Coordinator for USDA, 401 W. Peachtree St NW, Room 2328, Atlanta, GA 30308,

(ii) For all other audits conducted in accordance with § 1773.3 report to the appropriate office based on location. See <https://www.usda.gov/oig/national.htm> to determine the correct reporting location.

#### **§ 1773.10 Access to audit documentation.**

Pursuant to the terms of this part and the audit engagement letter, the auditor must make all audit documentation available to RUS, or its designated representative, upon request and must permit RUS, or its designated representative, to photocopy all audit documentation.

#### **§§ 1773.11–1773.19 [Reserved]**

### **Subpart C—RUS Requirements for the Submission and Review of the Reporting Package**

#### **§ 1773.20 The auditor’s submission of the reporting package.**

(a) *Time limit.* Within 90 days of the audit date, the auditor must deliver the reporting package to the auditee’s governance board. At a minimum, copies should be provided for each member of the governance board and the manager. The auditor must also provide an electronic copy of the audit which meets the requirements of § 1773.21 for subsequent transmittal to RUS.

(b) *Communication with the governance board.* In addition to providing sufficient copies of the reporting package for each member of the auditee’s governance board, RUS requires that the auditor report all audit findings to the auditee’s governance board. RUS recommends that audit findings also be communicated orally unless oral communication would not be adequate. If the information is communicated orally, the auditor must document the communication by appropriate memoranda or notations in the audit documentation. If the auditor communicates in writing, a copy of the written communication must be included in the auditor’s audit documentation.

(c) *Matters to be communicated.* Matters communicated to those charged

with governance must include, but are not limited to the matters to be communicated as prescribed in the AICPA’s professional standards AU-C Section 260, “The Auditor’s Communication with Those Charged with Governance”.

#### **§ 1773.21 Auditee’s review and submission of the reporting package.**

(a) The auditee’s governance board should note and record receipt of the reporting package and any action taken in response to the reporting package in the minutes of the board meeting at which such reporting package is presented.

(b) The auditee must furnish RUS with an electronic copy of the reporting package within 120 days of the audit date as provided for in § 1773.3.

(c) The auditee must furnish AA-PARA with a copy of its plan for corrective action, if any, within 180 days of the audit date.

(d) The auditee must include in the reporting package a copy of each special report, summary of recommendations or similar communications, if any, received from the auditor as a result of the audit.

(e) All required submissions to RUS described in paragraphs (b) through (d) of this section should be furnished electronically. The electronic copy must be provided in a Portable Document Format (PDF). Auditees with a designation from 0001 through 0199 in the Electric program and 500 through 699 in the Telecommunications programs shall upload the reporting package to the DCS or its successor system. Borrowers and/or grantees with a designation from 1100 through 1199, 1300 through 1399, and 1400 through 1499 in the Broadband program shall upload the reporting package to the BCAS or its successor system. All other borrowers and/or grantees may upload their reporting package through DCS or its successor system. Specific instructions for submission are available from the Technical Accounting and Auditing Staff.

#### **§§ 1773.22–1773.29 [Reserved]**

### **Subpart D—RUS Reporting Requirements**

#### **§ 1773.30 [Reserved]**

#### **§ 1773.31 Auditor’s report on the financial statements.**

The auditor must prepare a written report on comparative balance sheets, statements of revenue and patronage capital (or statement of operations customary to the type of entity reporting) and statements of cash flows.

The report must include the manual or printed signature of the auditor, cover all statements presented, and refer to the separate report on internal controls over financial reporting and on compliance and other matters and the report on compliance with aspects of contractual agreements and regulatory requirements issued in conjunction with the auditor’s report on the financial statements. The auditor’s report on the financial statements should also state that the report on internal controls over financial reporting and on compliance and other matters is an integral part of a GAGAS audit, and in considering the results of the audit, that this report should be read along with the auditor’s report on the financial statements.

#### **§ 1773.32 Report on internal control over financial reporting and on compliance and other matters.**

(a) As required by GAGAS, the auditor must prepare a written report describing the scope of the auditor’s testing of internal control over financial reporting and of compliance with provisions of laws, regulations, contracts, and loan and grant agreements, and that the tests provided sufficient, appropriate evidence to support opinions on the effectiveness of internal control and on compliance with provisions of laws, regulations, contracts, and loan and grant agreements. This report must include the manual or printed signature of the auditor and must include the following items as appropriate:

- (1) Significant deficiencies and material weaknesses in internal control;
- (2) Instances of fraud and noncompliance with provisions of laws or regulations that have a material effect on the audit and any other instances that warrant the attention of those charged with governance;
- (3) Noncompliance with provisions of contracts or grant agreements that have a material effect on the audit; and
- (4) Abuse that has a material effect on the audit.

(b) When the auditor detects instances of noncompliance or abuse that have an effect on the financial statements that are less than material but warrant the attention of those charged with governance, they should communicate those findings in writing to those charged with governance in a separate communication. If the auditor has issued a separate communication detailing immaterial instances of noncompliance or abuse, the report on internal controls over financial reporting and on compliance and other matters must be modified to include a statement such as:



“We noted certain immaterial instances of noncompliance [and/or abuse], which we have reported to the management of (auditee’s name) in a separate letter dated (month, day, 20XX).”

(c) If the auditor has issued a separate letter to management to communicate other matters involving the design and operation of the internal control over financial reporting, the report on internal controls over financial reporting and on compliance and other matters must be modified to include a statement such as:

“However, we noted other matters involving the internal control over financial reporting that we have reported to the management of (auditee’s name) in a separate letter dated (month, day, 20XX).”

(d) The report must contain the status of known but uncorrected deficiencies from prior audits that affect the current audit objective.

**§ 1773.33 Report on compliance with aspects of contractual agreements and regulatory requirements.**

The auditor must prepare a report on compliance with aspects of contractual agreements and regulatory requirements that includes, at a minimum, comments on:

(a) *Audit procedures.* State whether the audit has been performed in accordance with this part;

(b) *Special reports.* State whether any special reports, summaries of recommendations, or similar communications were furnished to the auditee’s management during the course of the audit or during interim audit work, and provide a description of the information furnished;

(c) *Accounting and records.* Comment on whether, during the course of the audit, anything came to the auditor’s attention to indicate that the auditee did not maintain adequate and effective accounting procedures and records and utilize adequate and fair methods for accumulating and recording labor, material, and overhead costs, and for distributing these costs to construction, retirement, and maintenance or other expense accounts. Where appropriate, comment on whether anything came to the auditor’s attention to indicate that the auditee did not:

(1) Establish continuing property records (CPRs) that are updated on a current basis, at least annually, and are reconciled with the controlling general ledger plant accounts;

(2) Promptly clear construction clearing accounts of costs of completed construction to the proper classified plant accounts and accrue depreciation

on such completed construction from the date the plant was placed in service;

(3) Currently and systematically record and properly price retirements of plant;

(4) Properly account for the accumulated provision for depreciation accounts associated with retirements of plant or properly disclose any unusual charges or credits to such accounts; and

(5) Obtain RUS approval for the sale, lease or transfer of capital assets secured under the RUS security agreement when approval is required, and properly handle any proceeds from the sale or lease of plant, material or scrap in conformance with RUS requirements.

(d) *Materials control.* Comment on whether, during the course of the audit, anything came to the auditor’s attention to indicate that the control over materials and supplies was not adequate.

(e) *Compliance with RUS loan and security instrument provisions.* Comment on whether, during the course of the audit, anything came to the auditor’s attention to indicate that the following provisions of RUS’ loan and security instruments have not been complied with:

(1) For electric auditees, provisions related to:

(i) The requirements for an auditee to obtain written approval of mortgagees to enter into any contract for the management, operation, or maintenance of the auditee’s system if the contract covers all or substantially all of the electric system. For purposes of this part, the following contracts shall be deemed as requiring RUS approval:

(A) Management contracts in which the auditee has contracted to have another auditee or other entity manage its affairs;

(B) Operations and maintenance contracts in which the auditee has contracted to have another auditee or other entity operate and/or maintain all or substantially all of the physical plant facilities of the auditee.

(C) Operations and maintenance contracts in which the auditee has contracted to operate and maintain the physical plant facilities of another auditee or other utility system;

(ii) The requirement for an auditee to prepare and furnish mortgagees annual or periodic financial and operating reports on the auditee’s financial condition and operations accurately and within the required deadlines. The auditor shall comment on whether, during the course of the audit, anything came to the auditor’s attention to indicate that the information represented by the auditee as having been submitted to RUS in its most

recent December 31 Financial and Operating Report Electric Distribution or Financial and Operating Report Electric Power Supply was not in agreement with the auditee’s audited records. If the auditee represents that an amended report has been filed as of December 31, the comments must relate to the amended report; and

(iii) The requirement for an auditee to use depreciation rates that are within the ranges established by RUS for each primary plant account (See RUS Bulletin 183–1, Depreciation Rates and Procedures at [https://www.rd.usda.gov/files/UPA\\_Bulletin\\_183-1.pdf](https://www.rd.usda.gov/files/UPA_Bulletin_183-1.pdf)), or with the requirements of the state regulatory body having jurisdiction over the auditee’s depreciation rates in computing monthly accruals.

(2) For telecommunications auditees, provisions related to:

(i) The requirement for an auditee to obtain written approval of the mortgagees to enter into any contract, agreement or lease between the auditee and an affiliate other than as allowed under 7 CFR part 1744, subpart E; and

(ii) The requirement for an auditee to prepare and furnish mortgagees annual or periodic financial and operating reports on the auditee’s financial condition and operations accurately and within the required deadlines. The auditor shall comment on whether, during the course of the audit, anything came to the auditor’s attention to indicate that the information represented by the auditee as having been submitted to RUS in its most recent December 31 Operating Report for Telecommunications Borrowers was not in agreement with the auditee’s audited records. If the auditee represents that an amended report has been filed as of December 31, the comments must be related to the amended report.

(3) For Broadband auditees, provisions relating to the requirement for an auditee to prepare and furnish mortgagee quarterly or periodic financial and operating reports on the auditee’s financial condition and operations accurately and within the required deadlines. The auditor shall comment on whether, during the course of the audit, anything came to the auditor’s attention to indicate that the information represented by the auditee as having been submitted to RUS in its most recent BCAS filing was not in agreement with the auditee’s audited records. If the auditee represents that an amended report has been filed, the comments must be related to the amended report.

(4) For grantees, provisions related to:



(i) Recipients of Broadband Initiatives Program loans and grants, the requirement for the recipient to prepare and furnish RUS quarterly and annual financial and operating reports on the financial condition and operations of the auditee accurately and within the required deadlines. The auditor shall comment on whether, during the course of the audit, anything came to the auditor's attention to indicate that the information represented by the auditee as having been submitted to RUS in its most recent BCAS filing was not in agreement with the audited records of the auditee. If the auditee represents that an amended report has been filed, the comments must relate to the amended report. The auditor must state whether the Annual Compliance Certificate required by the RUS Security Agreement has been filed in a timely manner with RUS.

(ii) Recipients of all other grant programs within the electric and telecommunications programs, the requirements to prepare and furnish RUS with any required financial reporting accurately and within required deadlines, as appropriate for that specific program. The auditor shall comment on whether, during the course of the audit, anything came to the auditor's attention to indicate that the information represented by the grantee as having been submitted to RUS in its most recent filing was not in agreement with the audited records of the grantee. If the grantee represents that an amended report has been filed, the comments must relate to the amended report.

(f) *Related party transactions.* Comment on whether, during the course of the audit, anything came to the attention of the auditor to indicate that all material related party transactions have not been disclosed in the notes to the financial statements in accordance with ASC 850, entitled "Related Party Disclosures".

(g) *Deferred debits and deferred credits.* For electric auditees, comment on whether, during the course of the audit anything came to the attention of the auditor to indicate that the auditee provided detailed schedule of deferred debits and deferred credits, including, but not limited to, margin stabilization plans, revenue deferral plans, and expense deferrals is not accurately presented. This schedule must be included as supplemental information or within the notes to the financial statements; and

(h) *Investments.* For electric and telecommunications auditees, comment on whether, during the course of the audit, anything came to the auditor's

attention to indicate that the auditee provided detailed schedule of investments is not accurately presented. This schedule must be included as supplemental information or within the notes to the financial statements. The auditor must state that the audit did not disclose any investments in subsidiary or affiliated companies.

#### **§ 1773.34 Schedule of findings and recommendations.**

The auditor must prepare a schedule of findings and recommendations to be included with the audited financial statements. The schedule of findings and recommendations shall be developed and presented utilizing the elements of a finding discussed in GAGAS and shall include recommendations for remediation. If the schedule does not include responses from management, as well as any planned corrective actions, those items must be submitted directly to the AA-PARA by management in accordance with § 1773.4(j).

#### **§§ 1773.35–1773.37 [Reserved]**

### **Subpart E—RUS Audit Requirements and Documentation**

#### **§ 1773.38 Scope of engagement.**

The audit requirements set forth in § 1773.39 through 1773.45 must be met annually by the auditor during the audit of the RUS auditee's financial statements. The auditor must exercise professional judgment in determining whether any auditing procedures in addition to those mandated by GAGAS or this part should be performed on the auditee's financial records in order to afford a reasonable basis for rendering the auditor's report on the financial statements, report on internal controls over financial reporting and on compliance and other matters, report on compliance with aspects of contractual agreements and regulatory requirements, and schedule of findings and recommendations.

#### **§ 1773.39 Utility plant and accumulated depreciation.**

(a) *General.* The audit of these accounts shall include tests of additions, replacements, retirements, and changes. The auditor's audit documentation shall support that the auditor:

(1) Examined direct labor and material transactions to determine whether the auditee's accounting records reflect a complete accumulation of costs;

(2) Examined indirect costs and overhead charges to determine if they conform to the Uniform System of

Accounts or the Federal Acquisitions Regulations as required under the RUS Security Agreement;

(3) Reviewed the costs of completed construction and retirement projects to determine if they were cleared promptly from the work in progress accounts to the classified plant in service accounts and the related depreciation accounts;

(4) Examined direct purchases of special equipment and general plant;

(5) Determined the degree of accuracy and control of costing retirements, including tests of salvage and removal costs;

(6) Reviewed the auditee's work order procedures; and

(7) Reviewed depreciation rates for adequate support, and compared them to RUS guidelines to determine that they were in compliance.

(b) *Construction work in progress.* (1) The audit documentation shall include a summary of open work orders reconciled to the general ledger and note on the summary any unusual or atypical projects.

(2) The auditor's audit documentation shall support that the auditor:

(i) Reviewed equipment purchases charged to work orders, including payments and receiving reports;

(ii) Reviewed contracts showing the scope of the work, the nature of the contract, the contract amount, and scheduled payments and reviewed supporting documents to determine that services contracted for were in fact rendered;

(iii) Reviewed time cards and pay rates for a sample of employees who allocate their time to work orders;

(iv) Reviewed the nature of material and supplies issued to the project, traced amounts and quantities to supporting documents, and reviewed the reasonableness of clearing rates for assignment of stores expense to the work order;

(v) Reviewed the accuracy of the computation of overheads applied to the work order; and

(vi) Reviewed other costs charged to the work order for support and propriety.

(3) The auditor's audit documentation shall support that the auditor:

(i) Scheduled payments to contractors and traced to verify payments and supporting invoices;

(ii) Traced contract costs to final closeout documents, to the general ledger, and to the continuing property records; and

(iii) Verified the costs of owner furnished materials, if applicable.

(4) The auditor shall review the auditee's procedures for unitization and classification of work order and contract

costs. The auditor's audit documentation shall support that the auditor:

(i) Reviewed the tabulation of record units for construction from the work order staking sheets to the tabulation of record units, to the unitization sheets, and to the continuing property records;

(ii) Reviewed the procedures for unitizing and distributing costs of completed construction to the plant accounts;

(iii) Verified that standard costs were being used;

(iv) Evaluated the basis for development of standard costs; and

(v) Determined that costs of completed construction were cleared promptly from work in progress accounts.

(c) *Continuing property records.* The auditor's audit documentation shall support that the auditor:

(1) Determined whether the subsidiary plant records agree with the controlling general ledger plant accounts;

(2) Noted differences in the audit documentation; and

(3) Commented, in the report on compliance with aspects of contractual agreements and regulatory requirements, on any discrepancies.

(d) *Retirement work-in-progress.* The auditor's audit documentation shall support that the auditor:

(1) Determined that plant retirements are currently and systematically recorded and priced on the basis of the continuing property records, and determined that costs of removal have been properly accounted for;

(2) Explained the method used in computing the cost of units of plant retired if continuing property records have not been established and determined whether costs appeared reasonable; and

(3) Determined the manner in which net losses due to retirements were accounted for and traced clearing entries to the depreciation reserve, the plant accounts, and the continuing property records.

(e) *Provision for accumulated depreciation.* The auditor's audit documentation shall support that the auditor:

(1) Verified the depreciation accruals for the period, including the depreciation base;

(2) Reviewed the basis of the depreciation rates, any change in rates and the reason for the change, and, if appropriate, determined whether the rates are in compliance with RUS requirements or with the requirements of the state regulatory body having jurisdiction over the auditee's depreciation rates;

(3) Reviewed salvage and removal costs; and

(4) Searched for unrecorded retirements.

(f) *Other reserves.* The auditor's audit documentation shall include an account analysis for all other material plant reserves, such as the reserve for the amortization of plant acquisition adjustments. The auditor's audit documentation shall support that appropriate tests of transactions were performed.

(g) *Narrative.* The auditor shall include in the audit documentation a comprehensive narrative on the scope of work performed, observations made, and conclusions reached. Matters covered in this narrative shall include:

(1) The nature of construction and other additions;

(2) The control over, and the accuracy of pricing retirements;

(3) The accuracy of distributing costs to classified utility plant accounts;

(4) An evaluation of the method of:

(i) Capitalizing the direct loadings on labor and material costs;

(ii) Distributing transportation costs and other expense clearing accounts; and

(iii) Capitalizing overhead costs;

(5) The tests of depreciation;

(6) A review of agreements such as those relating to acquisitions, property sales, and leases which affect the plant accounts; and

(7) Notations, if applicable, of RUS approval of property sales and the propriety of the disposition of the proceeds.

#### **§ 1773.40 Regulatory assets.**

The auditor's audit documentation shall support that the auditor tested whether all regulatory assets comply with the requirements of ASC 980. For Electric auditees only, the auditor's audit documentation shall support that all regulatory assets have received RUS approval.

#### **§ 1773.41 Extraordinary retirement losses.**

The auditor's audit documentation shall support that the auditor tested retirement losses, including any required approval by a regulatory commission with jurisdiction in the matter, or RUS, in the absence of commission jurisdiction.

#### **§ 1773.42 Clearing accounts.**

The auditor's audit documentation shall support that the auditor tested all clearing accounts and that transactions selected for testing were reviewed for proper allocation between expense and capital accounts.

#### **§ 1773.43 Capital and equity accounts.**

(a) *Capital stock.* For privately owned companies, the audit documentation shall include analyses of all stock transactions during the audit period. The auditor's audit documentation shall support that the auditor:

(1) Reviewed the subsidiary records and reconciled them to the general ledger control account;

(2) Reviewed authorizations and issuances or redemptions of capital stock for proper approvals by the governance board, stockholders, regulatory commissions and RUS, as required;

(3) Determined that transactions were made in accordance with the appropriate provisions of the articles of incorporation, bylaws, and RUS loan documents; and

(4) Determined that transactions were recorded in accordance with the Uniform System of Accounts.

(b) *Memberships.* For cooperative organizations, the audit documentation shall include an analysis of the membership transactions during the audit period. The auditor's audit documentation shall support that the auditor:

(1) Reviewed the subsidiary records and reconciled them to the general ledger control account; and

(2) Determined that transactions were made in accordance with the appropriate provisions of the articles of incorporation, bylaws, and RUS loan documents.

(c) *Patronage capital, retained earnings, margins, and other equities.* The audit documentation shall include an analysis of the patronage capital, retained earnings, margins and other equities, and any related reserve accounts. The auditor's audit documentation shall support that the auditor:

(1) Determined that the transactions were made in accordance with the appropriate provisions of the articles of incorporation, bylaws, RUS loan documents, Uniform System of Accounts, or orders of regulatory commissions;

(2) Traced payments to underlying support; and

(3) Determined whether, under the terms of the RUS security instrument, restrictions of retained earnings or margins are required and, if so, whether they have been properly recorded.

#### **§ 1773.44 Long-term debt.**

The auditor's audit documentation shall support that the auditor:

(a) Confirmed RUS, FFB, and RTB debt to the appropriate confirmation schedule (RUS Form 690, Confirmation

Schedule Obligation to the FFB; Form 614, Confirmation Schedule—Long-term Obligation to RUS; or, Confirmation Schedule for RTB Debt);

(b) Confirmed other long-term debt directly with the lender;

(c) Examined notes executed or cancelled during the audit period; and

(d) Tested accrued interest computations.

#### **§ 1773.45 Regulatory liabilities.**

The auditor's audit documentation shall support that all regulatory liabilities comply with the requirements of ASC 980. For electric auditees only, the auditor's audit documentation shall document whether all regulatory liabilities have received RUS approval.

#### **§§ 1773.46–1773.48 [Reserved]**

#### **§ 1773.49 OMB Control Number.**

The information collection requirements in this part are approved by the Office of Management and Budget (OMB) and assigned the OMB Control Number 0572–0095.

Date: April 30, 2018.

**Kenneth L. Johnson,**

*Administrator, Rural Utilities Service.*

[FR Doc. 2018–09501 Filed 5–4–18; 8:45 am]

**BILLING CODE P**

## **SMALL BUSINESS ADMINISTRATION**

### **13 CFR Part 120**

#### **RIN 3245–AG79**

### **Debt Refinancing in 504 Loan Program**

**AGENCY:** U.S. Small Business Administration.

**ACTION:** Final rule.

**SUMMARY:** This rule finalizes the interim final rule (IFR) that was published on May 25, 2016, to implement the debt refinancing program reauthorized by Section 521 of Division E of the Consolidated Appropriations Act, 2016. In response to comments received on the IFR, this final rule makes some additional revisions to the program's regulations with respect to the definition of Qualified debt, the requirements related to Eligible Business Expenses, the refinancing of Projects involving single or limited use properties, and the disbursement period.

**DATES:** This rule is effective June 6, 2018.

**FOR FURTHER INFORMATION CONTACT:** Linda Reilly, 504 Program Chief at [linda.reilly@sba.gov](mailto:linda.reilly@sba.gov) or 202–205–9949.

**SUPPLEMENTARY INFORMATION:**

## **I. Background Information**

The 504 Loan Program is an SBA financing program authorized under Title V of the Small Business Investment Act of 1958 (the “SBIAct”), 15 U.S.C. 695 *et seq.* The core mission of the 504 Loan Program is to provide long-term financing to small businesses for the purchase or improvement of land, buildings, and major equipment, in an effort to facilitate the creation or retention of jobs and local economic development. Under the 504 Loan Program, loans are made to small business applicants by Certified Development Companies (“CDCs”), which are certified and regulated by SBA to promote economic development within their community. In general, a project in the 504 Loan Program (a “504 Project”) includes: A loan obtained from a private sector lender with a senior lien covering at least 50 percent of the project cost; a loan obtained from a CDC (a “504 Loan”) with a junior lien covering up to 40 percent of the total cost (backed by a 100 percent SBA-guaranteed debenture); and a contribution from the Borrower of at least 10 percent equity.

The Small Business Jobs Act of 2010 (the “Jobs Act”), Public Law 111–240, 124 Stat. 2504, enacted on September 27, 2010, temporarily expanded the ability of a small business to use the 504 Loan Program to refinance certain qualifying debt. Prior to the Jobs Act, a 504 Project could include a refinancing component only if the project involved an expansion of the small business and the existing indebtedness did not exceed 50% of the project cost of the expansion. *See* 13 CFR 120.882(e). The temporary Jobs Act program authorized the use of the 504 Loan Program for the refinancing of debt where there is no expansion of the small business concern (the “Debt Refinancing Program”). That program expired on September 27, 2012.

Section 521 of Division E of the Consolidated Appropriations Act, 2016 (the “2016 Act”), Public Law 114–113, enacted on December 22, 2015, reauthorized the Debt Refinancing Program with three modifications:

(1) The Debt Refinancing Program shall be in effect only in those fiscal years during which the cost to the Federal Government of making guarantees under the Debt Refinancing Program and under the 504 Loan Program is zero;

(2) A CDC is required to limit its financings under the 504 Loan Program so that, during any fiscal year, new financings under the Debt Refinancing Program do not exceed 50% of the dollars the CDC loaned under the 504

Loan Program during the previous fiscal year. The 2016 Act provides that this limitation may be waived by SBA upon application by a CDC and after determining that the refinance loan is needed for good cause; and

(3) The alternate job retention goal authorized by the Jobs Act for the Debt Refinancing Program is eliminated.

On May 25, 2016, SBA published an interim final rule to implement the 2016 Act (81 FR 33123) and, with the “zero cost” requirement satisfied for fiscal year 2016, SBA began accepting applications for assistance under the Debt Refinancing Program on June 25, 2016, the effective date of the interim final rule. With the “zero cost” requirement satisfied for fiscal years 2017 and 2018, the Debt Refinancing Program has continued to be in effect without interruption. The regulations governing this program are found at 13 CFR 120.882(g).

## **II. Summary of Comments Received**

SBA received 49 comments during the comment period for the interim final rule, which closed on July 25, 2016. Of the comments received, 44, or 90%, were from Certified Development Companies, one was from a trade association, one was from a law firm, one was from a commercial real estate broker, one was from a financial institution, and one was from a private citizen. Below is a summary of the comments received.

### **A. Definition of Qualified Debt—Section 120.882(g)(15)**

The Jobs Act authorizes the refinancing of “Qualified Debt” which is defined to mean, among other factors, “indebtedness” that “was incurred not less than 2 years before the date of the application for assistance”, that “is a commercial loan”, and the proceeds of which were used to acquire an Eligible Fixed Asset. *See* section 502(7)(C)(III)(aa)(AA), (BB), and (DD) of the SBIAct. In imposing the two-year requirement, Congress clearly did not want the Debt Refinancing Program to apply to new loans (*i.e.*, loans less than two years old). In implementing this statutory requirement, the current regulations define “Qualified debt”, in part, as a “commercial loan . . . [t]hat was incurred not less than 2 years before the date of the application for the refinancing available under [the 504 Debt Refinancing Program]”. *See* 13 CFR 120.882(g)(15) (definition of “Qualified debt”). Debt that was refinanced through the execution of a new Note within the two year period would not be considered Qualified debt under the current regulations.