The second amendment relaxed ownership requirements of paragraph (f) of section 997.30 *Outgoing regulations* by allowing handlers to transfer peanuts to another handler or to domestic commercial storage facilities. Originally, paragraph (f) applied to the transfer of peanuts from one plant to another of a handler's plants or to commercial storage without having the peanuts PLI and certified as meeting quality requirements—provided that ownership was retained by the handler and that the transfer was only to points within the same production area.

The amendment extended the provisions of paragraph (f) to allow the transfer of peanuts from one handler's facility to another handler's facility for further handling. The relaxation allows handlers to make the most efficient use of other handling facilities without having to pay additional costs entailed in obtaining PLI and quality certification of the peanuts. Any peanuts so transferred are still subject to all applicable edible quality requirements before being disposed of for human consumption. Thus, the revisions to paragraph (f) of section 997.30 to include the transfer of peanuts between facilities of different handlers without quality certification and PLI at the time of transfer is continued in effect.

Similarly, the third amendment revised some PLI and certification requirements of paragraphs (a)(1), (a)(2) and (a)(3) of section 997.40 *Reconditioning and disposition of peanuts failing quality requirements.* Paragraph (a)(1) previously provided that a handler of failing quality, Segregation 1 shelled peanuts may have remilled, moved under PLI to a custom remiller, sold to another handler, or blanched such peanuts. Paragraph (a)(2) provided that such peanuts moved to blanching, or sold to another handler for blanching, had to be moved under PLI. Paragraph (a)(3) required peanut lots in such transactions to be accompanied by a valid grade certificate and moved under PLI. Peanuts so handled had to be kept separate and apart from other peanuts at the remilling, blanching or receiving handler facility.

Under the relaxed handling procedure, the peanuts do not have to be moved under PLI to the remiller, blancher, or receiving handler. Further, to be consistent with the changes in the Agreement regulations, peanuts so moved no longer have to be kept separate and apart from other peanuts at the remilling, blanching or receiving handler facility. Thus, the revisions to paragraphs (a)(1), (a)(2), and (a)(3) of section 997.40 by removing references to PLI and movement accompanied by valid certification are continued in effect. Additionally, the provisions added in the appropriate provisions to provide that the transferred peanuts do not have to be kept separate and apart at the receiving remilling, blanching, or handling facility remain in effect.

The Committee members, in proposing the changes in the Agreement provisions, believed that the more restrictive level of regulatory control for each peanut lot is no longer needed. The changes in this rule are based on the fact that current shelling, processing, remilling and blanching technologies are generally more efficient than in the past. The rule makes it more economical for handlers to use blanchers' and remillers' facilities which are generally operated more efficiently. These facilities are now located throughout the different production areas which also encourages their use.

The rule provides handlers more reconditioning flexibility by eliminating some certification requirements and PLI of peanuts and by reducing costs incurred during movement to different locations and facilities. The rule should improve handlers' competitive positions. Relaxing the regulations has allowed freer movement of peanuts and more efficient use of facilities. The relaxation of PLI and certification requirements has reduced the number of inspections and should result in lower costs to the entire industry. Fewer inspections are not expected to compromise the industry's quality control and lot identification objectives.

The interim final rule also added and updated addresses and telephone and facsimile numbers, where applicable, of approved aflatoxin testing laboratories and identified the contact point of the USDA Science Division headquarter's office. The laboratories perform chemical analyses required by the non-signatory handling regulations. This information is provided in paragraphs (c)(5)(i) and (ii) of section 997.30 *Outgoing regulation.* Nine of the laboratories are approved by the USDA/AMS Science Division and eight are approved by the Committee. Non-signatory handlers may send peanut samples to any laboratory on the list, per instructions specified in paragraph (c) of the outgoing regulation.

The interim final rule on these issues was published in the Federal Register on September 28, 1995 (60 FR 50083). That rule invited interested persons to submit written comments through October 30, 1995. No Comments were received and the Department is adopting as a final rule, without change, the provisions of the interim final rule.

In accordance with the Paperwork Reduction Act of 1988 (44 U.S.C. Chapter 35), information collection requirements that are contained in this rule have been previously approved by the Office of Management and Budget (OMB) and have been assigned OMB No. 0581–0163.

Based on the above, the Administrator of the AMS has determined that this final rule will not have a significant economic impact on a substantial number of small entities.

After consideration of all available information, it is found that this rule, as hereinafter set forth, will tend to effectuate the declared policy of the Act.

List of Subjects in 7 CFR Part 997

Food grades and standards, Peanuts, Reporting and recordkeeping requirements.

For the reasons set forth in the preamble, 7 CFR part 997 is amended as follows:

## PART 997—PROVISIONS REGULATING THE QUALITY OF DOMESTICALLY PRODUCED PEANUTS HANDLED BY PERSONS NOT SUBJECT TO THE PEANUT MARKETING AGREEMENT

Accordingly, the interim final rule amending 7 CFR Part 997 which was published at 60 FR 50083 on September 28, 1995, is adopted as a final rule without change.

Dated: December 26, 1995.

Sharon Bomer Lauritsen,

*Deputy Director, Fruit and Vegetable Division.*

[FR Doc. 96–24 Filed 1–2–96; 8:45am]

BILLING CODE 3410–02–P

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## Rural Utilities Service

## 7 CFR Part 1773

### RIN 0572–AA93

## Policy on Audits of RUS Borrowers

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

**ACTION:** Interim final rule with request for comments.

**SUMMARY:** The Rural Utilities Service (RUS) hereby amends its regulations on audits of RUS borrowers. This rule incorporates changes to the audit regulations necessitated by the 1994 revision of Government Auditing Standards (GAGAS), issued by the Comptroller General of the United States, United States General Accounting Office (GAO), effective for financial audits of periods ending on or after January 1, 1995 and by Statement on Auditing Standards (SAS) No. 74,

Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance, issued by the Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA), effective for fiscal periods ending after December 31, 1994.

This rule also clarifies the peer review requirements for certified public accountants (CPA) performing audits of RUS borrowers.

**DATES:** This rule is effective January 3, 1996. This rule applies to audits of periods ending on December 31, 1995, and thereafter.

Written comments must be received by RUS or carry a postmark or equivalent no later than March 4, 1996.

**ADDRESSES:** Submit written comments to Ms. Roberta D. Purcell, Chief, Technical Accounting and Auditing Staff, Borrower Accounting Division, Rural Utilities Service, Ag Box 1523, room 2221–S, U.S. Department of Agriculture, Washington, DC 20250, telephone number (202) 720–5227. RUS requires a signed original and three copies of all comments (7 CFR part 1700). All comments will be made available for inspection at room 2234 South Building during regular business hours (7 CFR 1.27(b)).

**FOR FURTHER INFORMATION CONTACT:** Ms. Roberta D. Purcell, Chief, Technical Accounting and Auditing Staff, Borrower Accounting Division, Rural Utilities Service, Ag Box 1523, room 2221–S, U.S. Department Of Agriculture, Washington, DC 20250, telephone number (202) 720–5227.

**SUPPLEMENTARY INFORMATION:**

## Executive Order 12866

This interim 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).

## Regulatory Flexibility Act Certification

The Administrator, RUS, has determined that the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) does not apply to this rule.

## Information Collection and Record Keeping Requirements

The reporting and recordkeeping requirements contained in the interim rule were approved by the Office of Management and Budget (OMB) pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35, as amended) under control number 0572–0095.

Send questions or comments regarding this burden or any other aspect of these collections of information, including suggestions for reducing the burden, to F. Lamont Hepppe, Jr., Deputy Director, Program Support Staff, Rural Utilities Service, Ag Box 1522, Washington, DC 20250–1522.

## National Performance Review

This regulatory action is being taken as part of the National Performance Review program to eliminate unnecessary regulations and improve those that remain in force.

## National Environmental Policy Act Certification

The Administrator, RUS, has determined that this 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 program described by this interim rule is listed in the Catalog of Federal Domestic Assistance Programs under number 10.850—Rural Electrification Loans and Loan Guarantees. This catalog is available on a subscription basis from the Superintendent of Documents, the United States Government Printing Office, Washington, DC 20402, (202) 512–1800.

## Executive Order 12372

This rule is excluded from the scope of Executive Order 12372, Intergovernmental Consultation. A Notice of Final Rule entitled Department Programs and Activities Excluded from Executive Order 12372 (50 FR 47034) exempts RUS electric loans and loan guarantees from coverage under this Order.

## Executive Order 12778

This rule has been reviewed under Executive Order 12778, Civil Justice Reform. This rule: (1) Will not preempt any state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule; (2) Will not have any retroactive effect; and (3) Will not require administrative proceeding before parties may file suit challenging the provisions of this rule.

## Background

Part 1773 implements the standard RUS security instrument provision requiring RUS borrowers 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 CPA, satisfactory to RUS, and accompanied by a report of such audit, in form and substance satisfactory to RUS. A report of the audit was defined in § 1773.1, General, to include the auditor's report, report on compliance, report on internal controls and management letter.

On January 6, 1994, RUS published a final rule amending part 1773, at 59 FR 657, that revised and clarified a provision of part 1773 that requires a certified public accountant (CPA) to state whether an electric borrower has complied with certain provisions of its loan and security instruments. The January 6, 1994 final rule also incorporated the illustrative management letter issued by the AICPA in a Technical Practice Aid dated November 11, 1992.

This rule amends part 1773 to comply with the 1994 revision of GAGAS. The 1994 revision of GAGAS adds three additional field work standards. It also provides guidance on reporting, required communications, and external quality control review.

The first additional standard requires CPAs to follow up on known, material findings and recommendations from previous audits. This standard is accomplished through compliance with § 1773.32(a) and § 1773.33 of the current regulation.

The second additional standard requires CPAs to design their audits to detect material noncompliance with contracts or grant agreements. Section 1773.9, Disclosure of Irregularities and Illegal Acts, requires CPAs to design the audit to include audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a material effect on the financial statement amounts and to extend audit procedures if there is an indication that an irregularity may have occurred. This rule revises the language of this section to include the supplemental standard to design the audit to detect material noncompliance with contracts or grant agreements as required by the 1994 revision of GAGAS.

The third additional standard requires CPAs to provide, in the working papers, sufficient information to allow an experienced auditor to locate the evidence supporting the CPA's significant conclusions and judgments. Section 1773.6, Audit Agreement, requires the CPA and borrower to enter into an audit agreement. Among the declarations that must be included in the audit agreement is a statement that the CPA will document the audit work performed in accordance with the professional standards of the AICPA and part 1773. This rule revises this section to incorporate the additional working paper requirements set forth in the 1994 revision of GAGAS.

The 1994 revision of GAGAS requires the CPA to communicate the auditor's responsibilities for consideration of internal controls and compliance with laws and regulations and to contrast those responsibilities with the additional procedures that could be performed and the additional assurances or opinions on the internal control structure or on compliance with laws and regulations that would result. This communication must be with the board of directors. This rule revises § 1773.6 to include this required communication.

Section 1773.6 also requires the audit agreement to include a statement that ''The borrower and CPA acknowledge that RUS regulations provide that if the borrower fails to have an audit performed and documented in compliance with GAGAS and this part, the borrower is in violation of its security instrument with RUS''. In response to our September 23, 1993, proposed rule, one CPA firm stated that this language exceeds the applicable mortgage covenant and the following language should be substituted ''The borrower and CPA acknowledge that RUS will consider the borrower to be in violation of its security instrument with RUS if the borrower fails to have an audit performed and documented in compliance with GAGAS and 7 CFR part 1773. The proposed rule published on September 23, 1993, did not include revisions to § 1773.6; therefore, we have incorporated the aforementioned revision in this proceeding.

Section 1773.5, Qualifications of CPA, requires a CPA to submit to a peer review of its accounting and audit practice every three years or at such additional times as designated by the peer review executive committee. Due to the increased number of peer reviews being performed, many reviewers have experienced problems scheduling peer reviews within the required time period. As a result, the AICPA extended the time period to 42 months. RUS is, therefore, amending its requirement to allow CPAs an additional six months to comply.

Similarly, the AICPA Board of Directors and the AICPA Council approved the combination of the peer review program conducted by the Private Companies Practice Section of the AICPA and the AICPA quality review program effective for reviews performed April 3, 1995, and thereafter. The AICPA Peer Review Board will conduct this program in cooperation with the state CPA societies. Section 1773.5 has been revised to reflect the changes necessitated by this merger.

The 1994 revision of GAGAS also provides guidance on external quality control (peer) reviews. The CPA is required to provide a copy of its most recent peer review report to those contracting for the audit. Reciprocal peer reviews are prohibited; for example, an audit organization is not permitted to review the organization that conducted its most recent review. This interim rule revises § 1773.5 to incorporate the aforementioned change.

RUS's peer review requirement as currently set forth in § 1773.5 does not allow individual CPAs that previously audited RUS borrowers as part of a CPA firm to enter into private practice and audit RUS borrowers without first obtaining a peer review. RUS is allowing the Administrator of RUS to waive the peer review requirement for a period of 18 months if the CPA meets certain proposed criteria set forth in § 1773.5(c)(7). The criteria established provides RUS with assurance that the CPA has previously participated in establishing the quality control standards for a CPA firm, the CPA has had responsibility for the audit of an RUS borrower, and that a CPA firm is not reorganizing for the sole purpose of evading the peer review requirement or extending the time period for the performance of a peer review.

The 1994 revision of GAGAS requires the auditor's report to refer to separate reports on compliance and on internal controls. Section 1773.31, Auditor's Report, requires the CPA to prepare a written report covering all statements issued. This rule revises the language of this section to incorporate the aforementioned change.

The 1988 revision of GAGAS required auditors to express positive-negative assurance on compliance with laws and regulations in the report on compliance and to identify the categories of controls considered significant in the report on the internal control structure. These requirements were eliminated in the 1994 revision of GAGAS. Section 1773.32, Report on Compliance, requires the CPA to prepare a written report on compliance with applicable laws, regulations, and contracts as required by GAGAS. This rule removes the positive-negative assurance requirement from the report on compliance. Similarly, § 1773.33, Report on Internal Controls, requires the CPA to prepare a written report on the borrower's internal control structure and the assessment of control risk made as part of the financial statement audit as required by GAGAS. This rule deletes the requirement to identify the categories of controls considered significant in the CPA's report on the internal control structure.

Section 1773.34, Management Letter, specifies the minimum requirements for the CPA's management letter. Among these is the requirement for the CPA to state whether the information submitted to RUS in its most recent December 31 RUS Form 7, Financial and Statistical Report; Form 12, Operating Report—Financial; or Form 479, Financial and Statistical Report for Telephone Borrowers, is in agreement with the borrower's records. This rule would clarify that the CPA's statement must indicate whether the most recent December 31 RUS Form 7, 12, or 479 agrees with the borrower's ''audited'' records.

The CPA is also required by § 1773.34 to comment when depreciation rates for electric borrowers are not in compliance with RUS requirements. This rule clarifies the requirement that the CPA comment when the depreciation rates used by the borrower for each primary plant account are not within the range established for that particular account by RUS Bulletin 183–1, Depreciation Rates and Procedures, or by the requirements of the state regulatory body having jurisdiction over the borrower's depreciation rates.

Also included in § 1773.34 is a requirement for the CPA to comment on the adequacy of the borrower's controls over materials and supplies. As part of the comment, RUS requires the presentation of a ''Detailed Schedule of Inventory Differences.'' RUS is eliminating this schedule as it does not provide information that is beneficial to the users of the financial statements. The above changes are also reflected in the revision of Appendix C to Part 1773—Illustrative Independent Auditor's Management Letter.

In February 1995, the Auditing Standards Board issued SAS No. 74, Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance, effective for fiscal periods ending after December 31, 1994. SAS No. 74 supersedes SAS No. 68, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance. In conjunction with the issuance of SAS No. 74 and the 1994 revision of GAGAS, the AICPA also revised its illustrative reports in the Audit and Accounting Guide, Audits of State and Local Governmental Units, thereby necessitating the changes in the sample reports contained in Appendix A to Part 1773—Sample Auditor's Report for an Electric Cooperative and Appendix B to Part 1773—Sample Auditor's Report for a Class A or B Commercial Telephone Company.

RUS has determined that, for a number of reasons, good cause exists to make this rule effective immediately on an interim basis. Notice and comment prior to the effective date is impractical, unnecessary and contrary to the public interest. RUS loan documents and implementing regulations generally require that each borrower provide RUS with an annual audit report, prepared by an independent CPA within 120 days of the ''as of'' audit date. To meet this deadline for audits of financial statements prepared as of December 31, 1995, audits must be undertaken immediately. In conducting the audit and preparing the report, CPAs are required to comply with the provisions of GAGAS and with the provisions of this part 1773. As a result of changes in GAGAS, there are currently inconsistencies between GAGAS and this part 1773; therefore, CPAs must be immediately advised of the applicable audit requirements and any inconsistencies between GAGAS and part 1773 must be resolved. If the inconsistencies are not resolved, borrowers could be placed in technical default under their loan documents with both the government and private co-lenders. Any failure to comply with loan documents can of course affect borrowers access to and cost of capital. Moreover, borrowers could be forced to incur additional audit expense absent an immediate reconciliation of RUS audit requirements. Such consequences are not in the interests of the RUS program, the borrowers or the people they serve. In addition, many of the changes implemented by this rule were previously subjected to notice and comment prior to being issued by GAO. Consequently, further notice and comment is unnecessary.

List of Subjects in 7 CFR Part 1773

Accounting, Electric power, Loan programs—communications, Loan programs—energy, Reporting and recordkeeping requirements, Rural areas, Telecommunications.

For the reasons set forth in the preamble, RUS hereby amends 7 CFR chapter XVII as follows:

## PART 1773—POLICY ON AUDITS OF RUS BORROWERS

1. The authority citation for Part 1773 continues to read as follows:

Authority: 7 U.S.C. 901 *et seq.;* 7 U.S.C. 1921 *et seq.*; Pub. L. 103–354, 108 Stat. 3178 (7 U.S.C. 6941 *et seq.*).

2. Section 1773.1 is amended by revising paragraph (c) to read as follows:

### § 1773.1 General.

* * * * *

(c) This part complies with the 1994 revision of Government Auditing Standards, issued by the Comptroller General of the United States, United States General Accounting Office.

* * * * *

3. Section 1773.5 is amended by revising paragraph (c) to read as follows:

### § 1773.5 Qualifications of CPA.

* * * * *

(c) *Peer review requirement.* The CPA must belong to and participate in a peer review program, and must have undergone a satisfactory peer review of the accounting and audit practice conducted by an approved peer review program under paragraph (c)(4) of this section, unless a waiver is granted under paragraph (c)(7) of this section. The reviewing organization must not be affiliated with or have had its most recent peer review conducted by the organization currently being reviewed (reciprocal reviews). After the initial peer review has been performed, the CPA must undergo a peer review of the accounting and audit practice within 42 months of the previous ''as of'' peer review date or at such additional times as designated by the peer review executive committee.

(1) A CPA that receives an unqualified peer review report will be satisfactory to RUS provided that the CPA meets the other criteria set forth in this section.

(2) If a CPA receives a qualified or adverse peer review report, the CPA must undergo a second peer review within 18 months of the date of the qualified or adverse report. A CPA that receives an unqualified second peer review report will be satisfactory to RUS provided that the CPA meets the other criteria set forth in this section.

(3) A CPA that receives a second qualified or adverse peer review report will not be satisfactory to RUS.

(4) Approved peer review programs. The following peer review programs are approved by RUS:

(i) The peer review programs conducted by the AICPA;

(ii) The peer review program conducted by the regulated audit program group of the National Conference of CPA Practitioners; and

(iii) An independent peer review program that, in RUS's determination, requires its members to:

(A) Ensure that the CPA can legally engage in the practice of certified public accounting;

(B) Adhere to the quality control standards established by the AICPA;

(C) Submit to peer reviews of the CPA's accounting and audit practice every 42 months or at such additional times as designated by its own executive committee; and

(D) Ensure that all professionals in the firm, including CPAs and nonCPAs, take part in the qualifying continuing professional education requirements of GAGAS, as set forth in paragraphs (c)(4)(iii)(D)(*1*) and (c)(4)(iii)(D)(*2*). A qualified continuing professional education course is one which meets the standards of the AICPA.

(*1*) An auditor responsible for planning, directing, conducting, or reporting on government audits must complete, every two years, at least eighty hours of continuing education and training which contributes to the auditor's professional proficiency. At least twenty hours must be completed in any one year of the two-year period; and

(*2*) An individual responsible for planning, directing, and conducting substantial portions of the field work, or reporting on the government audit must complete at least 24 of the 80 hours of continuing education and training in subjects directly related to the government environment and to government auditing. If the audited entity operates in a specific or unique environment, auditors must receive training that is related to that environment.

(5) *Notification.* The CPA must notify the Director, BAD, in writing, of participation in a peer review program. RUS will notify the CPA within 60 days of receipt of this notice if the selected peer review program is acceptable.

(6) *Submission of reports.* The CPA must submit to the Director, BAD, a copy of any peer review report and accompanying letter of comment, if any, within 60 days of the date such report and letter of comment are released by the peer review group.

(i) If the peer review report indicates that a follow-up review will be made, the CPA must submit subsequent reports to the Director, BAD, within 60 days of the date such reports are released by the peer review group.

(ii) A peer review report must be submitted to the Director, BAD, at least once every 42 months, or more frequently, if required by the peer review program.

(iii) A copy of the peer review report, accompanying letter of comment, and the partners' inspections must be made available to OGC, upon request.

(7) Waiver of the peer review requirement.

(i) A CPA may request that the Administrator, RUS, waive the peer review requirement. To be eligible for a waiver, the following criteria must be met:

(A) The firm has been in existence for less than 1 year from the date of the request and has not been previously organized under a different name;

(B) One of the partners organizing the firm has previously, within 18 months preceding the request, worked for a firm that has been peer reviewed and the partner was partner-in-charge of audits of RUS borrowers in the previous firm;

(C) The firm has enrolled in an approved peer review program; and

(D) The firm agrees to have the peer review conducted within 18 months of the date of the RUS waiver.

(ii) Waiver requests must address each of the criteria in paragraph (c)(7)(i) of this section and should be submitted to the Director, Borrower Accounting Division.

* * * * *

4. Section 1773.6 is amended by revising paragraph (a) to read as follows:

### § 1773.6 Audit agreement.

(a) An audit agreement must be entered into between the CPA and the borrower. The audit agreement must set forth the auditor's responsibilities in a financial statement audit, including the responsibilities for testing and reporting on internal controls and compliance with laws and regulations and the nature of any additional testing of internal controls and compliance required by laws and regulations. These responsibilities should be contrasted with the additional procedures that could be performed that would result in additional assurances or opinions on the internal control structure and compliance with laws and regulations. The audit agreement must also include the following:

(1) The borrower and the CPA acknowledge that the audit is being performed and the auditor's report, report on compliance, report on internal controls, and management letter is being issued in order to enable the borrower to comply with the provisions of RUS's security instrument;

(2) The borrower and CPA acknowledge that RUS will consider the borrower to be in violation of its security instrument with RUS if the borrower fails to have an audit performed and documented in compliance with GAGAS and this part;

(3) The CPA represents that he/she meets the requirements under this part to be satisfactory to RUS;

(4) The CPA will perform the audit and will prepare the auditor's report, report on compliance, report on internal controls, and management letter in accordance with the requirements of this part;

(5) The CPA will document the audit work performed in accordance with GAGAS, the professional standards of the AICPA, and the requirements of this part;

(6) The CPA will make all audit-related documents, including auditor's reports, workpapers, and management letters available to RUS or its representatives (OGC and GAO), upon request, and will permit the photocopying of all audit-related documents; and

(7) The CPA will follow the requirements of reporting irregularities and illegal acts as outlined in § 1773.9.

* * * * *

5. Section 1773.9 is amended by revising paragraphs (a) and (b) to read as follows:

### § 1773.9 Disclosure of irregularities and illegal acts.

(a) In accordance with GAGAS, the CPA must design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, illegal acts, and noncompliance with the provisions of contracts or grant agreements that could have a direct and material effect on financial statement amounts.

(b) If there is an indication that an irregularity may have occurred or evidence concerning the existence of a possible instance of noncompliance with the provisions of contracts or grant agreements that could have a material direct or indirect effect on the financial statements, the CPA must extend audit steps and procedures to obtain sufficient, competent evidential matter to determine whether, in fact, an irregularity or an instance of noncompliance has occurred and the effect on the borrower's financial statements.

* * * * *

6. Section 1773.31 is revised to read as follows:

### § 1773.31 Auditor's report.

The CPA must prepare a written report on comparative balance sheets, statements of revenue and patronage capital (or income and retained earnings, depending upon the structure of the borrower) and statements of cash flows. This report must be signed by the CPA, cover all statements presented, and refer to the separate reports on internal controls and on compliance with laws and regulations issued in conjunction with the auditor's report.

7. Section 1773.32 is amended by revising paragraph (a) to read as follows:

### § 1773.32 Report on compliance.

(a) As required by GAGAS, the CPA must prepare a written report on the tests performed for compliance with applicable laws, regulations, contracts, and grants. This report must be signed by the CPA and must contain the status of known but uncorrected significant or material findings and recommendations from prior audits that affect the current audit objective.

* * * * *

8. Section 1773.33 is revised to read as follows:

### § 1773.33 Report on internal controls.

As required by GAGAS, the CPA must prepare a written report on the borrower's internal control structure and the assessment of control risk made as part of the financial statement audit. This report must be signed by the CPA and must include, as a minimum:

(a) The scope of the CPA's work to obtain an understanding of the borrower's internal control structure and in assessing the control risk;

(b) A description of the reportable conditions noted which include material weaknesses identified as a result of the CPA's work in understanding and assessing the control risk; and

(c) The status of known but uncorrected, significant or material findings and recommendations from prior audits that affect the current audit objective.

9. Section 1773.34 is amended by removing paragraphs (d)(1), (d)(2), and (d)(3) and revising paragraphs (e)(1)(iii), (e)(2)(iii), and (g) to read as follows:

### § 1773.34 Management letter.

* * * * *

(e) * * *

(1) * * *

(iii) The requirement for a borrower to prepare and furnish mortgagees annual financial and statistical reports on the borrower's financial condition and operations. The CPA must state whether the information represented by the borrower as having been submitted to RUS in its most recent December 31 RUS Form 7 or Form 12 is in agreement with the borrower's audited records, and must comment on any exceptions noted. If the borrower represents that an amended report has been filed as of December 31, the comments must relate to the amended report.

(2) * * *

(iii) The requirement for a borrower to prepare and furnish mortgagees annual financial and statistical reports on the borrower's financial condition and operations. The CPA must state whether the information represented by the borrower as having been submitted to RUS in its most recent December 31 RUS Form 479 is in agreement with the borrower's audited records, and must comment on any exceptions noted. If the borrower represents that an amended report has been filed as of December 31, the comments must relate to the amended report;

* * * * *

(g) Depreciation rates. For electric borrowers, comment when the depreciation rates used in computing monthly accruals are not in compliance with RUS requirements (See RUS Bulletin 183–1, Depreciation Rates and Procedures), which require the use of depreciation rates that are within the ranges established by RUS for each primary plant account, or with the requirements of the State regulatory body having jurisdiction over the borrower's depreciation rates; and

* * * * *

10. In Appendix A to Part 1773 Exhibits 1 through 6 are revised to read as follows:

## Appendix A to Part 1773—Sample Auditor's Report for an Electric Cooperative

* * * * *

*Exhibit 1—Sample Auditor's Report*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center County Electric Cooperative:

Independent Auditor's Report

We have audited the accompanying balance sheets of Center County Electric Cooperative as of December 31, 19X9 and 19X8, and the related statements of revenue and patronage capital, and cash flows for the years then ended. These financial statements are the responsibility of Center County Electric Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Center County Electric Cooperative as of December 31, 19X9 and 19X8, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued a report dated March 2, 19X0, on our consideration of Center County Electric Cooperative's internal control structure and a report dated March 2, 19X0, on its compliance with laws and regulations.

Certified Public Accountants

March 2, 19X0

*Exhibit 2—Sample Report on Compliance When, Based on Assessments of Materiality and Audit Risk, the CPA Concluded It Was Not Necessary to Perform Tests of Compliance With Laws and Regulations*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center County Electric Cooperative:

We have audited the financial statements of Center County Electric Cooperative as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and the Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Center County Electric Cooperative is the responsibility of Center County Electric Cooperative's management. As part of our audit, we assessed the risk that noncompliance with certain provisions of laws, regulations, contracts, and grants could cause the financial statements to be materially misstated. We concluded that the risk of such material misstatement was sufficiently low that it was not necessary to perform tests of Center County Electric Cooperative's compliance with such provisions of laws, regulations, contracts, and grants.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 3—Sample Report on Compliance When, Based on Assessments of Materiality and Audit Risk, the CPA Performed Compliance Testing and Found No Reportable Instances of Noncompliance*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center County Electric Cooperative:

We have audited the financial statements of Center County Electric Cooperative as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Center County Electric Cooperative is the responsibility of Center County Electric Cooperative's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of Center County Electric Cooperative's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under Government Auditing Standards.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 4—Sample Report on Compliance When, Based on Assessments of Materiality and Audit Risk, the CPA Performed Compliance Testing and Found Reportable Instances of Noncompliance*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center County Electric Cooperative:

We have audited the financial statements of Center County Electric Cooperative as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Center County Electric Cooperative is the responsibility of Center County Electric Cooperative's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we preformed tests of Center County Electric Cooperative's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed instances of noncompliance that are required to be reported herein under Government Auditing Standards for which the ultimate resolution cannot presently be determined. Accordingly, no provision for any liability that may result has been recognized in Center County Electric Cooperative's 19X9 and 19X8 financial statements.

[Include paragraphs describing the instances of noncompliance noted.]

We considered these instances of noncompliance in forming our opinion on whether Center County Electric Cooperative's 19X9 and 19X8 financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles, and this report does not effect our report dated March 2, 19X0, on those financial statements.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 5—Sample Report on Internal Controls When Reportable Conditions Were Found*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center County Electric Cooperative:

We have audited the financial statements of Center County Electric Cooperative as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of Center County Electric Cooperative is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of Center County Electric Cooperative for the years ended December 31, 19X9 and 19X8, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgement, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

[Include paragraphs to describe the reportable conditions noted.]

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe none of the reportable conditions described above is a material weakness.

We also noted other matters involving the internal control structure and its operation that we have reported to the management of Center County Electric Cooperative in a separate letter dated March 2, 19X0.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record, and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 6—Sample Report on Internal Controls When No Reportable Conditions Were Found*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center County Electric Cooperative:

We have audited the financial statements of Center County Electric Cooperative, as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of Center County Electric Cooperative is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of Center County Electric Cooperative for the years ended December 31, 19X9 and 19X8, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operations that we consider to be material weaknesses as defined above.

However, we noted other matters involving the internal control structure and its operation that we have reported to the management of Center County Electric Cooperative in a separate letter dated March 2, 19X0.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record, and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

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11. In Appendix B to Part 1773, Exhibits 1 through 6 are revised to read as follows:

## Appendix B to Part 1773—Sample Auditor's Report for a Class A or B Commercial Telephone Company

* * * * *

*Exhibit 1—Sample Auditor's Report*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center Telephone Company:

Independent Auditor's Report

We have audited the accompanying balance sheets of Center Telephone Company as of December 31, 19X9 and 19X8, and the related statements of revenue and patronage capital, and cash flows for the years then ended. These financial statements are the responsibility of Center Telephone Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Center Telephone Company as of December 31, 19X9 and 19X8, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued a report dated March 2, 19X0, on our consideration of Center Telephone Company's internal control structure and a report dated March 2, 19X0, on its compliance with laws and regulations.

Certified Public Accountants

March 2, 19X0

*Exhibit 2—Sample Report on Compliance When, Based on Assessments of Materiality and Audit Risk, the CPA Concluded It Was Not Necessary to Perform Tests of Compliance With Laws and Regulations*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center Telephone Company

We have audited the financial statements of Center Telephone Company as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and the Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Center Telephone Company is the responsibility of Center Telephone Company's management. As part of our audit, we assessed the risk that noncompliance with certain provisions of laws, regulations, contracts, and grants could cause the financial statements to be materially misstated. We concluded that the risk of such material misstatement was sufficiently low that it was not necessary to perform tests of Center Telephone Company's compliance with such provisions of laws, regulations, contracts, and grants.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 3—Sample Report on Compliance When, Based on Assessments of Materiality and Audit Risk, the CPA Performed Compliance Testing and Found No Reportable Instances of Noncompliance*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center Telephone Company:

We have audited the financial statements of Center Telephone Company as of and for the years ended December 31, 19X9 and 19X8, and have issued our report dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Center Telephone Company is the responsibility of Center Telephone Company's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of Center Telephone Company's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under Government Auditing Standards.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 4—Sample Report on Compliance When, Based on Assessments of Materiality and Audit Risk, the CPA Performed Compliance Testing and Found Reportable Instances of Noncompliance*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center Telephone Company:

We have audited the financial statements of Center Telephone Company as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to Center Telephone Company is the responsibility of Center Telephone Company's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we preformed tests of Center Telephone Company's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed instances of noncompliance that are required to be reported herein under Government Auditing Standards for which the ultimate resolution cannot presently be determined. Accordingly, no provision for any liability that may result has been recognized in Center Telephone Company's 19X9 and 19X8 financial statements.

[Include paragraphs describing the instances of noncompliance noted.]

We considered these instances of noncompliance in forming our opinion on whether Center Telephone Company's 19X9 and 19X8 financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles, and this report does not effect our report dated March 2, 19X0, on those financial statements.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 5—Sample Report on Internal Controls When Reportable Conditions Were Found*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center Telephone Company:

We have audited the financial statements of Center Telephone Company as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of Center Telephone Company is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of Center Telephone Company for the years ended December 31, 19X9 and 19X8, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgement, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

[Include paragraphs to describe the reportable conditions noted.]

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe none of the reportable conditions described above is a material weakness.

We also noted other matters involving the internal control structure and its operation that we have reported to the management of Center Telephone Company in a separate letter dated March 2, 19X0.

This report is intended for the information of the audit committee, management, and Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record, and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

*Exhibit 6—Sample Report on Internal Controls When No Reportable Conditions Were Found*

Certified Public Accountants, 1600 Main Street, City, State 24105, The Board of Directors, Center Telephone Company:

We have audited the financial statements of Center Telephone Company, as of and for the years ended December 31, 19X9 and 19X8, and have issued our report thereon dated March 2, 19X0.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of Center Telephone Company is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of Center Telephone Company for the years ended December 31, 19X9 and 19X8, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operations that we consider to be material weaknesses as defined above.

However, we noted other matters involving the internal control structure and its operation that we have reported to the management of Center Telephone Company in a separate letter dated March 2, 19X0.

This report is intended for the information of the audit committee, management, the Rural Utilities Service, and supplemental lenders. However, this report is a matter of public record, and its distribution is not limited.

Certified Public Accountants

March 2, 19X0

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12. Appendix C to Part 1773 is revised to read as follows:

## Appendix C to Part 1773—Illustrative Independent Auditor's Management Letter

RUS requires that CPAs auditing RUS borrowers provide a management letter in accordance with § 1773.34. This letter must be signed by the CPA, bear the same date as the auditor's report, and be addressed to the borrower's board of directors.

Illustrative Independent Auditor's Management Letter

March 15, 19X6

Board of Directors, [Name of Borrower], [City, State].

We have audited the financial statements of [Name of Borrower] for the year ended December 31, 19X5, and have issued our report thereon dated March 15, 19X6. We conducted our audit in accordance with generally accepted auditing standards, Government Auditing Standards issued by the Comptroller General of the United States, and 7 CFR part 1773, Policy on Audits of Rural Utilities Service (RUS) Borrowers. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing our audit of the financial statements of [Name of Borrower] for the year ended December 31, 19X5, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

A description of the responsibility of management for establishing and maintaining the internal control structure and the objectives of and inherent limitations in such a structure is set forth in our independent auditors' report on the internal control structure dated March 15, 19X6, and should be read in conjunction with this report.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants.

A material weakness is a condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control structure and its operation that we consider to be a material weakness as defined above. [If a material weakness was noted, refer the reader to the independent auditors' report on internal control structure.]

7 CFR 1773.34 requires comments on specific aspects of the internal control structure, compliance with specific RUS loan and security instrument provisions, and other additional matters. We have grouped our comments accordingly. In addition to obtaining reasonable assurance about whether the financial statements are free from material misstatements, at your request, we performed tests of specific aspects of the internal control structure, of compliance with specific RUS loan and security instrument provisions, and of additional matters. The specific aspects of the internal control structure, compliance with specific RUS loan and security instrument provisions, and additional matters tested include, among other things, the accounting procedures and records, materials control, compliance with specific RUS loan and security instrument provisions set forth in 7 CFR 1773.34 (e)(1), [for telephone borrowers, 7 CFR 1773.34 (e)(2)], related party transactions, and depreciation rates. [For electric borrowers:] The additional matters tested also include a schedule of deferred debits and credits, upon which we express an opinion. In addition, our audit of the financial statements also included the procedures specified in 7 CFR 1773.38–.45. Our objective was not to provide an opinion on these specific aspects of the internal control structure, compliance with specific RUS loan and security instrument provisions, or additional matters, and accordingly, we express no opinion thereon.

No reports (other than our independent auditors' report, our independent auditors' compliance report, and our independent auditors' report on the internal control structure, all dated March 15, 19X6) or summary of recommendations related to our audit have been furnished to management.

Our comments on specific aspects of the internal control structure, compliance with specific RUS loan and security instrument provisions, and other additional matters as required by 7 CFR 1773.34 are presented below.

Comments on Certain Specific Aspects of the Internal Control Structure

We noted no matters regarding [Name of Borrower]'s internal control structure and its operation that we consider to be a material weakness as previously defined with respect to:

—The accounting procedures and records [list other comments];
—The process for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts [list other comments]; and
—The materials control [list other comments].

Comments on Compliance With Specific RUS Loan and Security Instrument Provisions

Management's responsibility for compliance with laws, regulations, contracts, and grants is set forth in our independent auditors' report on compliance dated March 15, 19X6, and should be read in conjunction with this report. At your request, we have performed the procedures enumerated below with respect to compliance with certain provisions of laws, regulations, and contracts. The procedures we performed are summarized as follows:

—Procedure performed with respect to the requirement to maintain all funds in institutions whose accounts are insured by an Agency of the Federal government:

1. Obtained information from financial institutions with which [Name of Borrower] maintains funds that indicated that the institutions are insured by an Agency of the Federal government.

—Procedures performed with respect to the requirement for a borrower to obtain written approval of the mortgagee to enter into any contract for the operation or maintenance of property, or for the use of mortgaged property by others [see 1773.34 (e)(2)(i) for additional telephone borrower requirements in accordance with 7 CFR 1773.34 (e)] for the year ended December 31, 19X5 of [Name of Borrower]:

1. Obtained and read a borrower prepared schedule of new written contracts entered into during the year for the operation or maintenance of its property, or for the use of its property by others as defined in § 1773.34 (e)(1)(ii) [§ 1773.34 (e)(2)(i) for telephone borrowers]

2. Reviewed Board of Director minutes to ascertain whether board-approved written contracts are included in the borrower-prepared schedule.

3. Noted the existence of written RUS [and other mortgagee] approval of each contract listed by the borrower.

—Procedure performed with respect to the requirement to submit RUS Form 7 or Form 12 [Form 479 for telephone borrowers] to the RUS:

1. Agreed amounts reported in Form 7 or Form 12 [Form 479 for telephone borrowers] to [Name of Borrower]'s records.

The results of our tests indicate that, with respect to the items tested, [Name of Borrower] complied, except as noted below, in all material respects, with the specific RUS loan and security instrument provisions referred to below. With respect to items not tested, nothing came to our attention that caused us to believe that [Name of Borrower] had not complied, in all material respects, with those provisions. The specific provisions tested, as well as any exceptions noted, include the requirements that:

—The borrower maintains all funds in institutions whose accounts are insured by an Agency of the Federal government [list all exceptions];
—The borrower has obtained written approval of the RUS [and other mortgagees] to enter into any contract for the operation or maintenance of property, or for the use of mortgaged property by others as defined in § 1773.34 (e)(1)(ii) [§ 1773.34 (e)(2)(i) for telephone borrowers] [list all exceptions]; and
—The borrower has submitted its Form 7 or Form 12 [Form 479 for telephone borrowers] to the RUS and the Form 7 or Form 12 [Form 479 for telephone borrowers], Financial and Statistical Report, as of December 31, 19X5, represented by the borrower as having been submitted to RUS is in agreement with the [Name of Borrower]'s audited records in all material respects [list all exceptions].

Comments on Other Additional Matters

In connection with our audit of the financial statements of [Name of Borrower], nothing came to our attention that caused us to believe that [Name of Borrower] failed to comply with respect to:

—The reconciliation of subsidiary plant records to the controlling general ledger plant accounts addressed at 7 CFR 1773.34 (c)(1) [list all exceptions];
—The clearing of the construction accounts and the accrual of depreciation on completed construction addressed at 7 CFR 1773.34 (c)(2) [list all exceptions];
—The retirement of plant addressed at 7 CFR 1773.34 (c)(3) and (4) [list all exceptions];
—Sales of plant material, or scrap addressed at 7 CFR 1773.34 (c)(5) [list all exceptions];
—The disclosure of material related party transactions, in accordance with Statement of Financial Accounting Standards No. 57, Related Party Transactions, for the year ended December 31, 19X5, in the financial statements referenced in the first paragraph of this report addressed at 7 CFR 1773.34 (f) [list all exceptions]; and
—For electric borrowers only: depreciation rates addressed at 7 CFR 1773.34 (g) [list all exceptions].

For Electric Borrowers Only: Detailed Schedule of Deferred Debits and Deferred Credits

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The detailed schedule of deferred debits and deferred credits required by 7 CFR 1773.34 (h) and provided below is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

[The detailed schedule of deferred debits and deferred credits would be included here. The total amount of deferred debits and deferred credits as reported in the schedule must agree with the totals reported on the Balance Sheet under the specific captions of ''Deferred Debits'' and ''Deferred Credits''. Those items that have been approved, in writing, by RUS should be clearly indicated.]

This report is intended solely for the information and use of the board of directors, management, and the RUS and supplemental lenders. However, this report is a matter of public record and its distribution is not limited.

Certified Public Accountants

Dated: December 19, 1995.

Jill Long Thompson,

*Under Secretary, Rural Economic and Community Development.*

[FR Doc. 96–93 Filed 1–2–96; 8:45 am]

**BILLING CODE 3410–15–P**

## NATIONAL CREDIT UNION ADMINISTRATION

### 12 CFR Part 707

### Truth in Savings

**AGENCY:** National Credit Union Administration (NCUA).

**ACTION:** Approval of Information Collection Requirements.

**SUMMARY:** On September 27, 1993, the National Credit Union Administration (NCUA) published a final rule on Truth in Savings (58 FR 50394). At that time, the NCUA had not yet submitted its application to the Office of Management and Budget (OMB) for approval of the information collection requirements found in the regulation (see 58 FR 50444, 9/27/93). On July 18, 1994, the NCUA published the collection requirements in the Federal Register (59 FR 36451), notifying the public that the requirements had been submitted to OMB for approval and seeking public comment on the requirements. The information collection requirements in the final rule were approved by the Office of Management and Budget on September 29, 1994. The control number assigned for this rule is 3133–0134. Notice of this approval appeared in the Federal Register on November 21, 1994 (59 FR 59899). The Federal Register determined that the notice was inadequate, hence this new notice is provided.

**EFFECTIVE DATE:** January 1, 1996.

**ADDRESSES:** Becky Baker, Secretary of the Board, National Credit Union Administration Board, 1775 Duke Street, Alexandria, VA 22314–3428.

**FOR FURTHER INFORMATION CONTACT:** Hattie Ulan, Special Counsel to the General Counsel, telephone: (703) 518–6540, at the above address.

By the National Credit Union Administration Board on December 27, 1995.

Hattie Ulan,

*Acting Secretary of the Board.*

[FR Doc. 96–46 Filed 1–2–96; 8:45 am]

**BILLING CODE 7535–01–M**

## DEPARTMENT OF TRANSPORTATION

### Federal Aviation Administration

### 14 CFR Part 35

**[Docket No. 94–ANE–60; Special Condition No. 35–ANE–02]**

### Special Conditions; Hamilton Standard Model 568F Propeller

**AGENCY:** Federal Aviation Administration, DOT.

**ACTION:** Final special conditions.

**SUMMARY:** These special conditions are issued for the Hamilton Standard Model 568F propeller with electronic propeller and pitch control system. The applicable regulations currently do not contain adequate or appropriate safety standards for constant speed propellers with electronic propeller and pitch control. These special conditions contain additional safety standards which the Administrator considers necessary to establish a level of safety equivalent to that established by the airworthiness standards of part 35 of the Federal Aviation Regulations (FAR).

**EFFECTIVE DATE:** February 2, 1996.

**FOR FURTHER INFORMATION CONTACT:** Martin Buckman, Engine and Propeller Standards Staff, ANE–110, Engine and Propeller Directorate, Aircraft Certification Service, FAA, New England Region, 12 New England Executive Park, Burlington, Massachusetts, 01803–5229; telephone (617) 238–7112; fax (617) 238–7199.

**SUPPLEMENTARY INFORMATION:**

Background

On January 26, 1994, Hamilton Standard applied for type certification for a new Model 568F propeller. The new propeller would use a new electronic propeller and pitch control system in place of the primary governor control and synchrophaser unit.

The existing propeller pitch control is monitored by a governor which senses propeller speed and adjusts the pitch to absorb the engine power and therefore maintains the propeller at the correct RPM. When the primary governor fails, the propeller pitch is controlled by an overspeed governor. This type of system is conventional and its airworthiness considerations are addressed by part 35 of the FAR's.

The FAA has determined that special conditions are necessary to certificate a Hamilton Standard electronic propeller and pitch control in place of the primary governor control and synchrophaser unit for the Model 568F propeller. A Notice of Proposed Special Conditions was published in the Federal Register on January 20, 1995 (60 FR 4114) for the Hamilton Standard Model 568F propeller with electronic propeller and pitch control system. This control is designed to operate a mechanical and hydraulic interface for the engine and propeller. It commands speed governing, synchrophasing and provides beta scheduling. Electronic propeller and pitch controls introduce potential failures that can result in hazardous conditions. These types of