

Business Investment Corporation

Annual Report for the Fiscal Year 2006-07



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Paper

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1. Message from the Vice-Chairperson

On behalf of the Board of Directors, I am pleased to present the 2006-07 annual report of the Business Investment Corporation to the Minister of Innovation, Trade and Rural Development.

The Business Investment Corporation directs the management of the investment portfolio of the Department of Innovation, Trade and Rural Development and administers new investments made through the Small and Medium-sized Enterprise (SME) Fund and the Small Business and Market Development Program. The Corporation also administers the Fisheries Loan Guarantee Program, in partnership with the Department of Finance, and the Shellfish Aquaculture Working Capital Fund.

In 2006-07, the Corporation continued to make solid contributions to small business development in the province. Investments under the SME Fund and the Small Business and Market Development Program totaled \$4.5 million, leveraging more than \$13.7 million. In addition, the Board managed the collection of \$2.7 million, which was reinvested in the SME revolving fund.

I would like to acknowledge and thank the outgoing Board members for their dedication and commitment to the Corporation in 2006-07 and thank the new Board of Directors for their service thus far. As well, the dedicated officials in the Department of Innovation, Trade and Rural Development work diligently to support the Board in the discharge of its mandate and their expertise and talents are greatly appreciated.



John Bennett

Vice-Chairperson, Board of Directors
Business Investment Corporation

2. Overview of the Business Investment Corporation

2.1 Mandate and Mission

The Business Investment Corporation supports the vision of the Department of Innovation, Trade and Rural Development of “a diversified, competitive economy with productive and prosperous people in all regions of the province.”

The Corporation’s mandate is to direct the management of the investment portfolio of the department and to administer new investments made through the Small and Medium-sized Enterprise Fund and the Small Business and Market Development Program; as well as the Fisheries Loan Guarantee Program and the Shellfish Aquaculture Working Capital Fund.

Legislative authority for the Business Investment Corporation resides in the *Business Investment Corporation Act*. The Corporation, as provided for in the *Act*, is responsible for:

“... making available and managing investments in small to medium sized private businesses, co-operatives, community development corporations and other enterprises for the purpose of creating employment opportunities for the people of the province.”

2.2 Background

The Business Investment Corporation was established under the authority of the *Business Investment Corporation Act* on April 1, 2002. The Business Investment Corporation is the successor to three former Crown corporations: Enterprise Newfoundland and Labrador Corporation, the Fisheries Loan Board and the Farm Development Loan Board.

The Business Investment Corporation operates as a Crown agency reporting to the Minister of Innovation, Trade and Rural Development.

2.3 Board of Directors

The affairs of the Corporation are managed by an independent Board of Directors appointed by the Lieutenant-Governor in Council. In February 2007, a new Board of Directors was appointed to the Corporation, which now comprises five private sector members and three senior public sector officials:

Chairperson Vacant

Vice-Chairperson Mr. John Bennett, Mount Pearl

Members Mr. Bob Healey, St. John's
 Ms. Mene Conley, Goose Bay
 Mr. Robert Marche, Corner Brook
 Dr. Marina Sexton, Norris Point
 Deputy Minister, Department of Finance
 Deputy Minister, Department of Business
 Deputy Minister, Department of Innovation, Trade and
 Rural Development

The Board met seven times in 2006-07 in order to fulfill its mandate. In addition, a sub-committee of the Board, the Corporate Transaction Committee, chaired by the Corporation's Vice-Chairperson, met bi-weekly or at the call of the Chair.

Remuneration

The remuneration of the Board consists of

- Chair: \$330 per meeting day;
- Vice-chair: \$285 per meeting day;
- Four private sector members; \$240 per person per meeting day; and
- Three public employees: no additional remuneration.

2.4 Administrative Support to the Corporation

The Corporation is responsible for the ongoing management and recovery of loans and investments made by the Corporation and its predecessor organizations. The Department of Innovation, Trade and Rural Development provides administrative support to the Corporation. The Corporation does not have its own staff. Administrative costs incurred by the Department of Innovation, Trade and Rural Development in support of the Corporation are not recorded as an expense in the Corporation's financial statements.

Departmental staff manages the accounting, billing and accountability activities that support investment disbursement and recovery. They manage and monitor revenue collections and maintain accounting records for the province-wide portfolio of loans, equity and grants.

2.5 Programs

The Business Investment Corporation provides funding to help start, revitalize and grow small and medium-sized businesses. It is responsible for the administration of the following programs:

Small and Medium-sized Enterprise Fund

The Small and Medium-sized Enterprise (SME) Fund provides loans and equity investments to small and medium-sized businesses, targeting specific growth sectors with particular emphasis on those businesses that have export potential and need assistance to enter or expand into external markets. The SME Fund is a revolving fund providing loans and equity investments to eligible businesses within Newfoundland and Labrador, which indicate a high probability of viability and sustainability.

Small Business and Market Development Program

This program provides contributions of up to \$25,000 on a matching basis to new entrepreneurs and expanding small businesses to help them acquire the necessary expertise to pursue new business ideas and markets in new growth areas of the economy. In the 2006-07 fiscal year, the program had a \$1.0 million budget.

Fisheries Loan Guarantee Program

This program supports the development of the province's independent fish harvesting sector by providing government guarantees, to a maximum of \$1.3 million, on loans through commercial banks for the purchase of new or used fishing vessels and new equipment for the improvement, rebuilding or alteration of existing vessels. The program is designed to help the independent fish harvesting sector take advantage of ongoing and emerging new opportunities in the fishery.

Shellfish Aquaculture Working Capital Fund (AWCF)

This program provides working capital loans to commercial mussel and other shellfish growers and processors, complementary to funding available through commercial credit sources and other established federal and provincial government programs. The \$1.5 million Fund was established in 2001 through two federal/provincial cost-shared economic development agreements and operates on a revolving fund basis.

3. Highlights and Accomplishments

Budget for Fiscal Year 2006-07

During fiscal 2006-07 the Small and Medium-sized Enterprise (SME) Fund assisted 33 enterprises and was sustained through prior advances carried forward from previous years from the Province and cash collections from the portfolio.

Funding for the Small Business and Market Development Program continued at \$1.0 million annually.

Appointment of the New Board of Directors

In February 2007, a new Board of Directors was appointed to the Business Investment Corporation. The Board now comprises five private sector members and three public sector members. The term of the new private sector Board members will expire in February 2010.

4. Activities

4.1 Program Activities

The Corporation committed \$3.47 million in 2006-07 through the Small and Medium-sized Enterprise Fund (Term and Equity), attracting \$10.36 million in additional funding from private and public business financing, to help start or grow 33 small businesses.

The Corporation committed \$1.08 million in 2006-07 through the Small Business and Market Development Program to 112 small businesses, attracting an additional \$3.26 million in other business financing to help entrepreneurs and small businesses pursue new business ideas and new markets for their products and services.

Total regional investments through the Small Business and Market Development Program and the Small and Medium-sized Enterprise Fund in 2006-07 were:

- Avalon: 24 investments totaling more than \$785,000.
- Eastern: 29 investments totaling more than \$410,000.
- Central: 17 investments totaling more than \$650,000.
- Western: 70 investments totaling more than \$2,630,000; and
- Labrador: 5 investments totaling more than \$82,000.

The Corporation approved \$4.1 million in new fisheries loan guarantees in 2006-07 through chartered banks to nine fish harvesting enterprises for the purchase of new fishing vessels or the purchase and/or renovation of used vessels to help them take advantage of ongoing and emerging new business opportunities in the fishery.

In 2006-07, the Corporation managed the Shellfish Aquaculture Working Capital Fund that had a budget of \$1.4 million invested in 18 enterprises. There were no new investments in this revolving fund during the fiscal year as there were insufficient funds available under the program in 2006-07.

At March 31, 2007, the investment portfolio of the Business Investment Corporation consisted of 1,176 accounts totaling \$57.1 million, which included outstanding principal and interest (please refer to Note 3 in the attached Financial Statements). There was an allowance for doubtful accounts of \$47.8 million, so the balance sheet value of the portfolio was \$9.3 million.

The Board also reviews and approves requests for fishery loan guarantees, which are then issued by the Department of Finance. At March 31, 2007, there were 119 guaranteed loans outstanding valued at \$36.7 million.

In 2006-07, there were no funds returned to the provincial treasury from payments relating to investments, as collections totaling \$2,766,782 were retained in the SME revolving fund for future investments.

4.2 Financial Statements

The audited financial statements for the Corporation are found in *Appendix A* of this report. They will be tabled in the House of Assembly in *Financial Statements of Crown Corporations, Boards and Authorities for the Year ending March 31, 2007*.

5. Opportunities and Challenges Ahead

Small and Medium-sized Enterprise Fund

Subsequent to the first full year of operation, the Department of Innovation, Trade and Rural Development facilitated a review of the Fund's policies and procedures, which involved consultation and input from all service providers within the department. Amendments were recommended and presented to the Board at its March 2007 Directors' meeting and the recommendations were implemented with a view to improving service delivery on behalf of clients, while meeting Government's objectives with respect to the Fund. Regular reviews of the Fund's policies and procedures will continue as the Corporation strives to maintain timely and relevant services to clients.

Accountability of the Fund

The Department is continuing to explore the feasibility of establishing a comprehensive assessment and accountability framework, including jobs created and net economic benefit to the provincial economy and treasury. It is anticipated that this will be completed in the next fiscal year in consultation with the Board.

Administrative Support to the Corporation

The Department continues to provide administrative support to the Corporation and commencing with the fiscal year ending March 31, 2008, it is proposed that a reasonable portion of these costs, paid by the Department, will be recognized and allocated in the Corporation's financial statements, as approved by the Board.

Appendix A: Financial Statements

BUSINESS INVESTMENT CORPORATION

FINANCIAL STATEMENTS

31 MARCH 2007



OFFICE OF THE AUDITOR GENERAL
St. John's, Newfoundland and Labrador

AUDITOR'S REPORT

To the Board of Directors
Business Investment Corporation
St. John's, Newfoundland and Labrador

I have audited the balance sheet of the Business Investment Corporation as at 31 March 2007 and the statements of equity, revenues and expenses, and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance 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.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at 31 March 2007 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

A handwritten signature in blue ink, appearing to read "John L. Noseworthy".

JOHN L. NOSEWORTHY, CA
Auditor General

St. John's, Newfoundland and Labrador
18 May 2007

BUSINESS INVESTMENT CORPORATION
INDEX TO FINANCIAL STATEMENTS
31 March 2007

Balance Sheet	Statement 1
Statement of Equity	" 2
Statement of Revenues and Expenses	" 3
Statement of Cash Flows	" 4

BUSINESS INVESTMENT CORPORATION
BALANCE SHEET
31 March

2007

2006

ASSETS

Cash (Note 2)	\$ 14,628,006	\$ 13,266,173
Loans and equity investments (Note 3)	9,313,036	8,297,869
Long-term investments (Note 4)	9,422	9,422
	\$ 23,950,464	\$ 21,573,464

LIABILITIES AND EQUITY

Borrowers' deposits	\$ 68,517	\$ 68,517
Equity	23,881,947	21,504,947
	\$ 23,950,464	\$ 21,573,464

Contingent liabilities (Note 5)
Commitments (Note 6)

See accompanying notes

Signed on behalf of the Board:



 Chairperson



 Director of Portfolio Management

BUSINESS INVESTMENT CORPORATION
STATEMENT OF EQUITY
For the Year Ended 31 March

2007

2006

Contributed capital (Note 7)

Balance, beginning of year	\$ 65,356,559	\$ 59,764,839
Aquaculture Working Capital Fund reserve (Note 2)	3,800	816
Capital contributions from the Province	1,000,000	10,800,000
Contributions disbursed as grants	(607,485)	(464,487)
Principal written off, net of recoveries (Note 3)	(1,956,255)	(4,744,609)
Balance, end of year	63,796,619	65,356,559
Deficit		
Balance, beginning of year	(43,851,612)	(48,440,513)
Excess of revenues over expenses (expenses over revenues)	1,980,685	(155,708)
Principal written off, net of recoveries (Note 3)	1,956,255	4,744,609
Balance, end of year	(39,914,672)	(43,851,612)
Equity, end of year	\$ 23,881,947	\$ 21,504,947

See accompanying notes

BUSINESS INVESTMENT CORPORATION
STATEMENT OF REVENUES AND EXPENSES
For the Year Ended 31 March

2007

2006

	2007	2006
REVENUES		
Interest on loans	\$ 1,014,826	\$ 768,091
Other investment income	557,174	314,855
Recovery in value of loans receivable and equity investments (Note 3)	413,068	-
Dividend income	-	5,753
	<u>1,985,068</u>	<u>1,088,699</u>
EXPENSES		
Provision for decline in value of loans receivable and equity investments (Note 3)	-	1,244,122
Miscellaneous expense	4,383	285
	<u>4,383</u>	<u>1,244,407</u>
Excess of revenues over expenses (expenses over revenues)	\$ 1,980,685	\$ (155,708)

See accompanying notes

BUSINESS INVESTMENT CORPORATION
STATEMENT OF CASH FLOWS
For the Year Ended 31 March

2007

2006

Cash flows from operating activities

Excess of revenues over expenses (expenses over revenues)	\$ 1,980,685	\$ (155,708)
Adjustments for non-cash items		
Provision for decline (recovery) in value of loans receivable and equity investments	(413,068)	1,244,122
	<u>1,567,617</u>	<u>1,088,414</u>

Cash flows from investing activities

Increase in loans and equity investments	(3,368,881)	(3,055,577)
Collection of loans and equity investments	2,766,782	2,886,320
	<u>(602,099)</u>	<u>(169,257)</u>

Cash flows from financing activities

Aquaculture Working Capital Fund reserve	3,800	816
Capital contributions from the Province	1,000,000	10,800,000
Contributions disbursed as grants	(607,485)	(464,487)
	<u>396,315</u>	<u>10,336,329</u>

Net increase in cash 1,361,833 11,255,486

Cash, beginning of year 13,266,173 2,010,687

Cash, end of year \$ 14,628,006 \$ 13,266,173

See accompanying notes

BUSINESS INVESTMENT CORPORATION
NOTES TO FINANCIAL STATEMENTS
31 March 2007

Authority

The Business Investment Corporation (the Corporation) was established under the authority of the *Business Investment Corporation Act*. The Corporation is funded by the Province of Newfoundland and Labrador (the Province) and is responsible for making available and managing investments in small to medium sized private businesses, co-operatives, community development corporations and other enterprises for the purpose of creating employment opportunities for the people of the Province. The affairs of the Corporation are managed by a Board of Directors appointed by the Lieutenant-Governor in Council.

The *Business Investment Corporation Act* came into force effective 1 April 2002. Under this *Act*, the Business Investment Corporation was incorporated and became the successor to Enterprise Newfoundland and Labrador Corporation, the Fisheries Loan Board and the Farm Development Loan Board. Also under this *Act*, the *Fisheries Loan Act*, the *Farm Development Loan Act*, the *Economic Recovery Commission Act* and the *Enterprise Newfoundland and Labrador Corporation Act* were repealed.

1. Significant accounting policies

These financial statements have been prepared by the Corporation's management in accordance with Canadian generally accepted accounting principles. Outlined below are the significant accounting policies followed.

(a) Loans receivable

The Corporation records loans receivable at cost. When loans are identified as impaired, the Corporation records an allowance to reduce their carrying values to their estimated realizable amounts. Estimated realizable amounts are measured at discounted cash flows when the cash flows can be estimated with reasonable reliability, or alternatively, at the estimated net realizable value of the underlying security.

(b) Equity investments

The Corporation records equity investments at cost. In certain circumstances, the Corporation may have acquired the right to appoint representatives to an equity investee's board of directors or it may have a significant influence on the strategic operating, investing and financing policies of the investee. However, because of the nature of the Corporation's investment process and the manner in which these positions were acquired, such control or significant influence may not in fact be exercised or the Corporation may not intend to maintain such positions. Accordingly the Corporation's equity investments for all companies in which the Corporation holds voting rights are accounted for on the cost basis.

Provision is made by the Corporation for any decline in the value of investee companies which is considered to be other than temporary.

BUSINESS INVESTMENT CORPORATION
NOTES TO FINANCIAL STATEMENTS
31 March 2007

1. Significant accounting policies (cont.)

(c) Revenue recognition

Interest income is accounted for on the accrual basis for all loans other than the impaired portion of loans. Recognition of interest in accordance with the terms of the original loan agreement ceases when a loan becomes impaired. A loan is classified as impaired when, in the opinion of management, there is reasonable doubt as to the ultimate collectability of a portion of principal or interest, or when payment is contractually past due 90 days. The impaired portion of loans may revert to accrual status only when principal and interest payments have become fully current again, at which time any interest will be recognized in that fiscal year.

Dividends are recorded as income when received.

2. Aquaculture Working Capital Fund

On 30 March 2001, Enterprise Newfoundland and Labrador Corporation, a predecessor of the Corporation, entered into an agreement with the Federal and Provincial Governments to set up the Aquaculture Working Capital Fund (AWCF). The AWCF assists individuals and companies in the shell fish industry throughout the Province through repayable loans. The AWCF is a revolving fund in which the Corporation retains the loan repayments for future aquaculture loans until the conclusion of the agreement. The agreement is scheduled to conclude on 31 March 2011, extendable for 3 years, at which time the Corporation will reimburse all monies to the Federal and Provincial governments based on the proportions of their contribution.

To date the Corporation has received funding totalling \$1.5 million based on contributions of \$1.3 million in Federal funding from the Canada/Newfoundland Strategic Regional Diversification Agreement, and \$160,000 Federal and \$40,000 Provincial funding from the Canada/Newfoundland Agreement on Economic Renewal Agreement.

As at 31 March 2007, the AWCF had 18 loans outstanding totalling \$1,392,563 (2006 - 19 loans totalling \$1,473,326). During 2003-04 the Corporation established a separate loan portfolio and bank account to administer the AWCF and assist in identifying payments that are received and held for future loans. As at 31 March 2007, the AWCF had a balance of \$174,107 (2006 - \$76,475) which is included in these financial statements as cash.

3. Loans and equity investments

The determination of whether a loan is impaired and the appropriate carrying value of equity investments, involves significant judgement. The estimation of an appropriate allowance for decline in value of loans receivable and equity investments necessarily involves the use of estimates. These financial statements represent management's best estimates based on available information.

BUSINESS INVESTMENT CORPORATION
NOTES TO FINANCIAL STATEMENTS
31 March 2007

3. Loans and equity investments (cont.)

Loans and equity investments consist of the following:

	<u>2007</u>	<u>2006</u>
Loans receivable		
Principal due and unpaid	\$ 19,383,227	\$ 21,276,315
Principal not yet due	14,917,978	14,470,691
Interest due and unpaid	2,645,675	2,489,279
	36,946,880	38,236,285
Less: allowance for decline in value	(28,412,414)	(30,704,742)
	8,534,466	7,531,543
Equity investments		
Equity investments, at cost	20,160,320	20,763,889
Less: allowance for decline in value	(19,381,750)	(19,997,563)
	778,570	766,326
Loans and equity investments	\$ 9,313,036	\$ 8,297,869

The allowance for the decline in value of loans receivable and equity investments consists of the following:

	<u>2007</u>	<u>2006</u>
Balance, beginning of year	\$ 50,702,305	\$ 55,497,891
Principal written off, net of recoveries	(1,956,255)	(4,744,609)
Interest written off, net of recoveries	(538,818)	(1,295,099)
Provision for decline (recovery) in value of loans receivable and equity investments	(413,068)	1,244,122
Balance, end of year	\$ 47,794,164	\$ 50,702,305

The allowance for decline in value represents the Corporation's best estimate of future probable losses with respect to the loans receivable and equity investments. The Corporation recognizes that future economic and industry conditions are not predictable and therefore, their impact on the future cash flows anticipated is uncertain. Consequently, adjustments to the allowance are possible depending on the impact of these future events and management's best estimate of them.

BUSINESS INVESTMENT CORPORATION
NOTES TO FINANCIAL STATEMENTS
31 March 2007

4. Long-term investments

Long-term investments consist of 673 shares of Sun Life Financial Services of Canada Incorporated which were given to the Corporation as a result of the demutualization of Sun Life Assurance Company of Canada. The carrying value of the shares are recognized at the fair market value of \$9,422 as determined by the share price at the time of the transfer of shares to the Corporation. The fair market value of these shares as at 31 March 2007 was \$35,346 (2006 - \$33,414).

5. Contingent liabilities

- (a) A client of the Corporation has taken legal action as a result of certain alleged technical problems that the client claims to have experienced with a vessel that was financed through the Fisheries Loan Board Program. The amount of this potential claim is in the \$900,000 to \$1,100,000 range. In a matter related to this legal action, another party has been awarded a claim of \$1,800,000. The Province will not appeal this decision.
- (b) A statement of claim has been served on the Corporation by a company claiming a breach of contract. The company is claiming special damages of \$811,040, other general and unspecified damages, interest and costs associated with the action. The likelihood of loss as a result of this claim is not determinable.

6. Commitments

The Corporation has outstanding commitments in respect of approved but not yet disbursed loans, equity investments and/or grants in the amount of \$4,330,631 (2006 - \$2,854,343).

7. Contributed capital

The Corporation receives capital contributions from the Province and the Government of Canada for the purpose of making loans, equity investments, and providing business and market development grants. The Corporation depends on these capital contributions to carry out its mandate.

Contributed capital is reduced by the principal portion of loans collected and paid to the Province, the principal portion of loans written off, and by contributions which the Corporation disburses as grants under its Business and Market Development Program.

BUSINESS INVESTMENT CORPORATION
NOTES TO FINANCIAL STATEMENTS
31 March 2007

8. Financial instruments

The Corporation's financial instruments recognized on the balance sheet, in addition to the long-term investments described in Note 4, consist of cash, loans and equity investments, and borrowers' deposits. The carrying values of cash, and borrowers' deposits approximate current fair value due to their nature and the short-term maturity or current market rate associated with these instruments.

The Corporation's loans and equity investments are recognized on the balance sheet at cost with provision being made for any decline in their value. Any estimated impairment of these loans and equity investments has been provided for through an allowance for decline in value and no further credit risk exists for these items. The carrying value of loans and equity investments approximates discounted value of expected receipts. Therefore, their carrying values approximate their current fair value and these instruments are not subject to any material interest rate risk.

9. Related party transactions

The Corporation is administered as a division of the Department of Innovation, Trade and Rural Development. Expenses of \$587,062 (2006 - \$507,807) related to salaries, accommodations and administration are paid directly by the Department and no provision is made in these financial statements to reflect those expenditures.

10. Economic dependence

As a result of the Corporation's reliance on Provincial funding, the Corporation's ability to continue viable operations is dependent upon the decisions of the Province.

11. Income taxes

The Corporation is a Crown entity of the Province of Newfoundland and Labrador and as such is not subject to Provincial or Federal income taxes.