Technological Innovation Studies Program

Research Report

A STUDY OF
VENTURE CAPITAL FINANCING
IN CANADA

by

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School of Business Administration,
University of Western Ontario.
June, 1973

Rapport de recherche

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CHAPTER 1

THE SUPPLY OF VENTURE CAPITAL IN CANADA

Introduction

The Canadian Federal Government report "Foreign Direct Investment in Canada", commonly known as the Gray Report, states as one of its conclusions "that the (Canadian capital) markets show evidence of weaknesses and gaps in respect of risk taking and entrepreneurship".[1] It lists these gaps and weaknesses. The first two are "Venture Capital for New and Small Firms", and "Expansion Capital for Small and Medium-Sized Canadian Controlled Firms". The Gray Report further states, "There is not necessarily a lack of funds available for filling each of the categories of needs outlined above. In some cases, there may be investors who are prepared to advance sufficient funds to meet a particular demand, but for one reason or another the process of bringing the borrower and the lender together is not carried out satisfactorily. This in itself is evidence of a weakness in the allocative function of the markets".[2] The report also concludes that "the shortage of entrepreneurship in the financial industry frustrates the kind of industrial intermediation - the drawing together of financing and all the many other components to bring a new enterprise into being - which could permit a larger proportion of major projects to be undertaken in Canada by Canadians".[3]

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1. Op. cit., page 92.
2. Op. cit., page 92.
3. Op. cit., page 93.

This and other claims that venture capital is lacking and that the process of providing ventural capital is not carried out satisfactorily provided the impetus for this study. The purpose here is to document a) what venture capital is available in Canda, b) from what sources and 3) on what terms, and 4) to investigate whether or not users and potential users of venture capital have had difficulty in finding such capital. Unfortunately, the Gray report provided little documentation or supporting evidence to substantiate its claims.

A further objective is to investigate the role that Canada's financial institutions have played in the provision of this capital and to investigate whether government regulations or tax laws hinder their activity in the venture capital market to any significant degree.

Definition of Venture Capital

To begin our study on venture capital we first attempted to define it. We began with the definition of venture capital as equity capital provided for the start of a new business. It quickly became obvious that this definition was much too restrictive, especially since most of the organizations we interviewed prefer not to invest in firms at the start-up phase, or at least not strictly at the start-up phase. We therefore modified our definition of venture capital to include investments in "established firms".

We also asked for a definition of venture capital from the individuals and firms interviewed. The variety of answers which we expected and received tended to indicate a variety of levels at which these people were involved in the supply of venture capital.

In addition, many of the venture capital firms prefer to invest via debt as well as equity. This debt is often convertible into equity or accompanied by warrants and options for equity, but most venture capital investments seemed to include some debt. Most of this debt was unsecured or with very little security.

We therefore chose to define venture capital and the limits of our study as broadly as possible. We define it to be the provision of unsecured debt or equity capital for the growth of small businesses at any stage prior to their going public. We realize that some highly speculative public issues may be considered as venture capital. However, investigating this area would mean interviewing all investment dealers in Canada who play a role in the provision of private placements and speculative new issues. We have, therefore, ruled this topic out as venture capital. Readers desiring material on new issues should consult Shaw's article on new issues in Canada.[3.]

Objectives of the Study

The prime objective of this first phase of the study was to undertake a detailed survey of venture capital sources in Canada in an attempt to discover on what terms venture capital

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3. Shaw, D.C., "The Cost of Going Public in Canada", Financial Executive, July, 1969.

is available, the types of investment for which it is available and from what sources. It was not possible to interview individuals or small groups who are not formally incorporated for providing venture capital. But these investors constitute perhaps the majority of sources of funds which are oriented towards the start-up of new enterprises. Unfortunately, these groups are often ad hoc syndicates who invest jointly once and never again. We therefore concentrated on formally incorporated firms in Canada which tend to specialize in the provision of venture capital as we have defined it. These included some firms who were mainly involved in managing portfolios of public securities, but who devoted part of their resources to unsecured investments in non-public companies. Most of these firms, such as mutual funds and pension funds, had separate funds for the venture capital end of their business, which tended to become involved in ventures to some extent, although as a very small proportion of their investments. However, most of the venture capital investments of financial institutions are made through companies whose primary activity is the provision of venture capital. We attempted to cover these secondary sources where possible by interviewing the primary sources, namely the venture capital companies in which they had invested. An example here would be investment houses and banks who are shareholders in venture capital companies in Canada and who invest in new ventures and non-public companies primarily through this source.

The main questions asked were how much venture capital is available, on what terms is it available, for what types of investment is it available and are there obvious gaps in the provision of such capital. We also investigated the attitude of these companies towards government assistance programs and the role of the federal government in venture capital in Canada. We found that venture capital suppliers were quite interested in this topic, especially since they had recently formed an association of venture capitalists in Canada, the main purpose of which seems to be to "lobby" the federal government in an attempt to obtain government funds for investment in small businesses in parallel with their own private funds. This arrangement would be similar to the Small Business Investment Companies in the United States discussed later in this report.

We have therefore attempted to take a snapshot view of venture capital sources in Canada as of the spring of 1973. One of the problems of this survey approach is that the market is continually changing, and some firms which we initially detected as being suppliers of venture capital claimed they were no longer in the business, while other firms entered the market during our study, perhaps without being detected. A further problem with the study is that it represents the Canadian venture capital industry as venture capitalists describe it. This is not necessarily a fully accurate picture, especially since they tend to present mainly the optimistic side of venture capital. We present a summary of the responses which we obtained. Hopefully, these form at least a skeleton view of the venture capital market in Canada.

Importance of the Study

Several reasons for undertaking this study, in addition to the interests of the Province of Ontario, were:

a) The importance of small firms in manufacturing in that they are frequently the means by which new products and new processes are introduced into the market.

b) To ensure that facilities for small business financing are available so that they can compete for their share of scarce capital.

c) To promote the growth of small businesses so that they can attain a size required for effective competition.

d) A policy of promoting small business growth as a means for promoting Canadian ownership and control.

We have used the opportunity for generating course materials for a new program in small business and entrepreneurship at the School of Business Administration at the University of Western Ontario. A final justification is that we have had many requests from former students who were seeking funds to either start or maintain their own businesses. We were often at a loss to suggest sources other than the Industrial Development Bank and one or two other firms of which we were aware. We assume this is a common problem to entrepreneurs in general, as they are often not informed of the variety of sources of venture capital available to them. Unfortunately, the names of the firms interviewed must be kept confidential, as they have requested it.

Research Methodology

There are several different types of venture capital firms in Canada. We shall concentrate on four different types, which we shall call "finders", "packagers", "silent partners", and "primary" venture capital sources. The first of these, "finders", are individuals and firms whose only contribution is to put the entrepreneur or small business in contact with a likely source of venture capital. They are not too popular with venture capitalists, who refer to them as "the five percenters", since the finder typically charges five percent of the amount of financing obtained in return for that service. Some of the firms we originally contacted turned out to be finders, but we very quickly disregarded such firms when we learned their true role. Many of these are chartered accountants, lawyers and investment consultants who specialize in government sources of capital as well. The second type called a "packager" or "broker" provides a much more valuable service to entrepreneurs and small businesses in Canada. The role of such firms is essentially to evaluate proposals for venture capital and select those which they consider most promising. The "packager" usually assists the entrepreneur in compiling his proposal to make it as complete as possible. He then approaches sources of capital to obtain funds for the entrepreneur. The "packager" usually also invests some of his own funds, but this is often a small proportion of the total funds required. Other sources of capital at this stage are shareholders in the "packager" and these shareholders often include banks, trust companies, investment dealers, mutual funds and pension funds. The "packager" is then a form of "clearing house" for the entrepreneur who may never meet the actual sources of his capital. The third type, whom we have called "silent partners", include the institutions mentioned above who do not do the actual evaluation of venture capital proposals themselves. In addition, there are several sources of private capital in Canada such as family-owned capital generated by existing family-owned businesses. These families and their firms often prefer to invest as "silent partners" as well. We interviewed many of the "silent partner" type of investor during the study, but we preferred to concentrate on the primary source of capital through which they invested. The final category was the type of firm at which this study was aimed. This is the firm which supplies its own capital or the separate funds of its shareholders for venture capital investments in small businesses. It usually does its own evaluation of these proposals, and often invests the whole amount required. It may, however, invest jointly with other venture capital organizations, or with "silent partners". In fact, there seemed to be a trend towards more joint ventures among the firms we interviewed, as many managers indicated that they sought partners for investments where possible.

Once we detected venture companies we sent them an enquiry asking whether they would be willing to participate in our study and detailing what our objectives were. Sources of such leads were many and varied, but the primary ones were a venture capital symposium held in Toronto in January of 1971 as the original meeting to form the association of venture capitalists and a venture capital seminar held in Toronto in 1970. In addition, many individuals, companies and colleagues suggested firms, all of whom we contacted. In many cases, these firms were not directly involved with venture capital but we pursued every lead we obtained. We are reasonably confident that we have interviewed most of the incorporated sources of venture capital in Canada.

We found a total of 50 Canadian firms involved in the provision of venture capital. The geographical distribution of these was: Toronto 23, Montreal 20, Vancouver 4, and 3 elsewhere in Canada. The vast majority of their investments was in the Toronto area.

We designed a questionnaire and sent it to these companies asking various questions concerning their role in venture capital. The questionnaire was pretested on several companies and was divided into two main sections. The first section included questions which were easily answered, usually in numerical form. These include questions concerning how many investments the company had and the amount of these investments. The other type of question involved more complex, controversial and opinion-oriented topics. This meant that they were questions which were not easily answered and we concentrated on these questions at a follow-up interview with these companies. Examples of this type of question are (1) What requirements do you prefer in a proposal for venture capital funds? and (2) What should be the role of government in the provision of venture capital in Canada?

In addition, we interviewed eleven American venture capital firms using the same questionnaire to see if they were significantly different in their responses from Canadian companies.

Survey Results

The results of this survey are detailed in Tables 1 and 2 and summarized in Tables 3 to 28. We shall discuss additional questions which are not reported in those tables.

The company definitions of venture capital confirmed our decision to redefine venture capital broadly. Responses ranged from companies who specialized in investments in start-up of new ventures to companies who never invested in a firm until it had demonstrated at least five years of profitable performance. In fact, most companies preferred to invest in "established" firms rather than at the start-up phase as shown in Table 3. We found that the majority of venture capital sources interviewed were formed in 1969 or 1970, although a few had existed from the early fifties. Companies did not explain in detail where they found their proposals. Many replied that they had their own contacts in the industry who referred proposals to them, but the majority of them claimed that most proposals "just walk in the door". Most of the venture capitalists claimed they did not depend heavily on institutions for leads or referrals.

Type and Location of Investment

We found that venture capital companies tended to be located in Ontario mainly and to specialize in high technology as a type of investment as shown in Tables 4 and 7. They had no particular preferences for size or age of company in many cases, except for those who required a "track record" before they would invest in a company. The typical range of venture capital investments seemed to run from about fifty thousand dollars to about two hundred and fifty thousand dollars. As Table 9 illustrates, some investments fall outside this range, particularly on the high end. But most venture capitalists claim they prefer to invest in the vicinity of two hundred thousand dollars in any one investment as shown in Table 17. This figure may have been reduced recently because of the trend towards joint ventures. As mentioned earlier, venture capitalists seem to be much more willing to participate in joint ventures with other venture capital sources than in the past.

The forms of investment used tended to vary, with convertible debentures and convertible preferred being popular. Debentures tend to be used mainly as an instrument to which the venture capital investor can attach various covenants to control the behavior of the management when he does not have equity control of the company. Another reason for using debt was that many of the venture capitalists wished to obtain a return on their investment during the whole period of the investment including the early stages. This was naturally more the case for investments in "established" companies who were showing a profit. Table 12 shows the forms of investment used by the various companies. In addition, the desired amount of equity which the venture capitalists wish to acquire is listed in Table 13. Their attitude towards referring ventures to other venture capital companies was investigated and replies suggested that they will refer proposals to other sources if they are worthwhile but simply do not fit their own firm's current preferences.

Most of the venture capital companies also provided additional management services for the companies in which they invested as illustrated in Table 14. In some cases these were limited to financial advice, but in most cases the venture capital firm provided a whole spectrum of management assistance. The majority of them charged a fee, often paid in the form of common stock, for their services, as illustrated in Table 15.

The types of return expected on the investments are shown in Tables 1 and 2 and range from about ten percent compounded per year up to a maximum of about sixty percent compounded. Companies were often unwilling to discuss the amount of money they had available for investments, and we found informally that many of them are approaching the limits of their available funds as shown in Tables 18 and 19.

Profitability

The replies of venture capital companies regarding the percentage of their ventures which were profitable or unprofitable imply that they are very optimistic, in most cases, at the time of the investment. But many of them, as illustrated in Tables 21, 22 and 23, did not disclose a desired ratio of profitable to unprofitable companies. Most of the companies interviewed claimed that there are really three types of investment. These included the ones that were extremely profitable and those which were extremely unprofitable, both of which were easily identifiable.

But the majority of such investments tend to be the mass in the middle or the non-performers, called in the vernacular "the living dead". These companies continually require more and more funds and the venture capitalists are often unwilling to write them off since they still have potential to perform. Venture capitalists typically wish to maintain their investment until the company is capable of issuing equity to the public. But most of them replied that if the price were right they would sell their investment before a public issue was feasible. There was considerable difference in the expected time before an investment could issue stock to the public, as illustrated in Table 25. This is apparently as a result of the various preferences of the companies interviewed, since those specializing in start-up investments would express a much longer time horizon before taking a venture public than would those who preferred to invest in "established" companies.

Information is not available to evaluate the overall profitability of venture capital firms in Canada. The primary reason for this is that many of them have been in existence for too short a period of time for their investments to develop. In the United States, however, several studies[4] have shown that American venture capital firms have provided a relatively low return on investment (5-10%), especially when one considers the risk of their investments. The older venture capital firms in Canada have not

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4. Unpublished Report of Small Business Administration on SBIC Performance, 1973. (Range of return on investment from -3.6% to 9.5%, 1968 - 1972.

produced superior returns, but they have typically been more conservative, investing in established companies, both public companies and firms just prior to going public. The fact that all these Canadian venture capital firms are private, or subsidiaries of public firms, means that information is not available upon which to make an assessment of their financial performance.

Management Ability

The main problem raised by all of the venture capitalists was that there is definitely a lack of capable venture management in the companies which brought proposals to them. They expressed the belief that there was a shortage of "venture management" in Canada rather than a shortage of venture capital. This was also the attitude of American companies responding to the question of whether there was any significant difference between American ventures they normally assessed and any Canadian ventures they may have seen in the past. They replied that there seemed to be a significant difference in the management ability present in the venture proposals they received with Canadian management lagging behind that in the U.S. They hastened to add that this was even more distinct in Europe where managers typically have a very good technical background but tend to lack a mangement background. However, Canadian firms used this reason to explain the fact that many of their investments were located in the U.S.A.

The background of officers in venture capital firms was typically financial. Most of them had experience in the financial community. There was also a smaller proportion who had previous management experience in a particular industry. But most of them had little experience in the high technology industries, in which they prefer to invest. This may justify the criticism of many users that venture capitalists were not capable of evaluating their firms adequately because of their lack of expertise in high technology.

In answering our questions regarding assessing the risk of a particular venture, companies did use the high level of risk as their reason for not investing in the start-up stage of new ventures. But typically their response was that the judgment of the risk of a particular venture was based strictly on "gut feel" rather than any quantitative data. They also replied that assessed risk of the particular proposal and the desire to have covenants on their investment determined the particular mixture of debt and equity which they tended to use in a venture.

In terms of assessing proposals, the venture capitalists were unanimous in their agreement that assessing management ability was the key factor in every proposal analysis and this talent was perhaps the most difficult to find in venture proposals.

<u>Export Orientation</u>

Another criterion used by venture capital suppliers to assess proposals was that the firm must be capable of marketing its product in the U.S. or overseas as well as Canada. This meant it should appeal to a market greater than the Canadian alone to show sufficient growth potential for them to invest. This resulted in a preference expressed by many venture capital suppliers for investments in the U.S.

Several firms stated that 90% of their funds was invested in American companies. They claimed the quality of management present in these American firms was better than evidenced in Canadian firms. But another reason stated by over half of the suppliers was that these firms had better access to the American market because of the lack of restrictive tariffs facing Canadian firms exporting to the U.S. Other reasons advanced by venture firms for investing in the U.S. were cheaper construction and distribution costs, availability of skilled labour and the large number of other investors willing to invest in joint ventures in the U.S.

It was also learned that several ventures which were originally Canadian have been financed on the condition that they incorporate and build facilities in the U.S. to gain some of the advantages listed above. These are rare, but illustrate the preference for American firms.

Control of Investments

Most of the venture capital companies had similar controls and monitoring systems for their investments. It was standard procedure to have a representative of the venture capital firm on the Board of Directors of the companies in which they had investments. In addition, other controls tended to include weekly or monthly reports during the early phases of an investment and quarterly or annual reports as the investment matured, and close contact by telephone and visits to the company whenever possible. Most firms placed covenants on the investment, usually on the debt instruments with which they invested in the company. Typical covenants usually enable them to monitor and control these investments through approval over any salary changes, approval of major expenditures above a certain level and approval of any dividends or other outflows of cash. Some companies limit the management of the firms in which they had investments by requiring cheque signing power and allowing the management little or no decision making power except for routine day to day operations. In fact, some companies expressed that their objective was to run the company and manage it completely. But the majority of the venture capital companies were primarily interested in monitoring their investment, and some of them wished to have as little contact with the company as possible, since their time was valuable and direct involvement on previous occasions had taught them how demanding such activity could be on their time.

Of the users questioned, many claim that they, or acquaintances who had funds from a venture capital company, had been "choked to death" by the control stranglehold which some venture capital companies imposed. It is this close monitoring and control which often tends to scare off entrepreneurs from using venture capital obtained from these companies, since the typical entrepreneur is not the type of individual who wants to be closely constrained.

It is also significant that relatively few professionals operate the venture capital organizations as illustrated by Table 20.

They evaluate a tremendous number of proposals each year and, on the average, invest in less than one percent of these proposals. These executives also claim a large number of proposals are rejected during the first five minutes of a telephone conversation and many others do not pass the initial screening of a ten or fifteen minute meeting with a venture capital representative. The same personnel typically perform the evaluations as well as monitoring their investments. Since their time available for monitoring is limited, the controls must be "automatic" to a great extent.

The total number of proposals investigated by venture capital firms has grown tremendously during the last five years. Thirty-one of the fifty suppliers interviewed were formed during this period so that the capacity of the industry for venture evaluation has presumably more than doubled. The firms interviewed all stated that they were assessing more proposals than ever before.

Other firms suggested that their monitoring consisted mainly of setting milestones or goals for the companies in which they had an investment. They typically made investments in the company on an installment basis subject to the firm meeting these milestones in each case. For example, a company which required two hundred thousand dollars might get half of the amount at first and if they met certain objectives over the next six months, they would get the additional amount of money. Otherwise they would not get it or it would be invested only on more expensive terms than the previous amount had been invested.

Comparison of American and Canadian Venture Suppliers

The replies to questions from American and Canadian venture capital firms, are similar; however, the focus for this study is on the major differences.

American firms were more willing to invest in the early development stage of a business than were Canadian firms as shown in Tables 3 and 4. We later found in our user survey that American firms invested in some Canadian businesses which had been refused by Canadian venture capitalists because they lacked "a track record".

American firms typically had more investments than Canadian firms and were more willing to invest amounts less than $100,000 as illustrated in Tables 3 and 4.

Those American firms which had used American government financing had typically done so as a Small Business Investment Company under the Small Business Administration. This is a program whereby venture capital firms are licensed as SBIC's and can borrow money from the American government or raise public funds with government guaranteed debentures. The concept will be discussed later in terms of its implications if applied in Canada.

Conclusions and Recommendations

When asked whether there is a shortage of venture capital in Canada, most of the venture capitalists interviewed responded that for a good project there was no problem in raising capital. Even those firms which had exhausted their current supply of funds stated that they could easily find other investors for the "right" deal. However, they did acknowledge that the vast majority of proposals which were brought to them probably did not receive financing from any source. Whether these proposals were all of the type which deserved to "die a quiet death" and never be heard from again is debatable. There was general agreement among venture capitalists that many otherwise good ventures never did find financing because they did not have capable management to undertake them.

It was our conclusion that the greatest problem for the entrepreneur seeking funds was to determine who supplied venture capital and on what terms, and which venture capital supplier would be the most likely to be interested in his particular proposal. It was a very difficult process for us to find them. There is apparently no public information available on this subject in Canada, so that the individual seeking funds is usually at a loss regarding possible sources of funds. We found that bank managers, accountants and lawyers were of little help in assisting the entrepreneur or the small firm by recommending potential sources of capital, except for those who have become "finders" of venture capital. In fact, we found that many of the venture capital firms intentionally play "hard to get". They justify this by saying that the type of entrepreneur they are seeking is the kind who can, as they put it, "see through the forest to the trees".

From our enquiries of users of venture capital, we receive a definite "yes" to the question, "Is there a lack of venture capital in Canada?" They were of the opinion that the venture capital which is available is first of all hard to detect and second, available only on very expensive terms. Their phrase for this was that venture capitalists want "an arm and a leg" in return for their money. They said there is definitely a lack of venture capital in Canada, especially at the start-up and early development stages, and especially on terms that the small businessman could afford.

It was our conclusion that there is definitely a lack of venture management in Canada, since this was the reason most ventures were unable to obtain funds from venture capital sources. The fact that venture capitalists are currently attempting to interest the federal government in a joint effort to provide venture capital on terms similar to the Small Business Investment Company program in the U.S. seems to affirm the responses that there was a lack of venture capital in Canada. They seem to be attempting to increase the amount of capital available by having the government provide an equal amount in parallel to that provided from private sources. There is a definite lack of venture capital for the start-up and development phases.

We are recommending for future study an investigation of the Small Business Investment Company program in the U.S. to detect the strengths and weaknesses there before Canada embarks on a similar program. In addition, we conducted a study of the user side of venture capital. The user phase is described in the next chapter.

In summary, we have presented an aggregate response to questions directed at sources of venture capital in Canada and, although we were unable to disclose the names of these companies, it represents the only summary of such information that we have seen on Canadian companies.

AMERICAN COMPANIES TABLE 3.1

Company	1	2	3	4	5	6	7	8	9	10	11
Started	1970	1952	1969	1969	1962	1962	1956	1921	1960	1946	1970
Will invest in	Start-up Development Expansion Acquisition	Start-up Development Expansion	Develop. Expansion Turn-around Acquisition	Start-up Development	Start-up Development Expansion	Start-up Turn-around	Start-up Development Turn-around	Start-up Development Expansion	Development Expansion Acquisition	Start-up Development Expansion	Development Expansion
Industries Preferred	Manufacturing	No	No	No	Related to Ocean	Electonics, Computor Systems	No	None	Pollution Control	None	Electronics Computers
Industries Avoided	None	Steel & utilities	—	No	—	—	—	—	If highly dependent on skills	None	None
Other Preferences	High technology	—	Low technology	High Technology	—	High Technology	High Technology	None	—	High Technology	High Technology
Areas Preferred	West Coast of U.S.	—	None	West Coast of U.S.A.	None	West Coast of U.S.	United States	U.S.,Canada Eur.& Aust.	East Coast U.S.	U.S.,Europe Canada	California U.S
Areas Avoided	None	Latin Am. Far East	None	Other than West,U.S.	If Pol. unstable	Distance is factor	Overseas Mexico	Yes	None	None	Europe Asia
Range of Investments	$100,000-250,000 250,000-500,000	$20,000-250,000	$20-50,000 50-100,000 100-250,000 250-500,000	$100,000-250,000	$20,000-250,000	$5,000-1,000,000	$10-20,000 250,000-500,000	$20,000-100,000	$20,000-1,000,000	—	$50,000-100,000
Investments Made in Range	5 1	25	4 4 2 4	8	20	41	1 8	150	20	—	1
Maximum Investment Considered	$500,000	$250,000	—	$500,000	Unlimited	$600,000	$300,000	$100,000	$750,000	—	$100,000
Form of Investing	Common, Convert. Deventure Warrants Options	Common, Convertible Pre Convert. Debenture Debt	Common, Convertible Debenture	Common Shares	Combination of equity & debt	Combination of Equity & debt with conversion rights	Equity	equity & debt	Conversion Debs with warrants	Combination of debt and equity	Warrants Options Debt
Equity Preferred	Not require control	Require control as group	Do not require control	Do not require control	Do not require control	Do not require control	voting control	Do not require control	Do not require control	Do not require control	Require Control
Provide Management Services	Yes	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes on a minor scale	Yes
Charge for Services	No	No	Yes	—	No	No	No	Yes	Yes	Yes Flat fee	No
Current Investments	6	20	14	8	10	30	9	20	—	47	1
Average Investment	$150,000	$150,000	$300,000	$175,000	—	$275,000	$200,000	$75,000	$300,000	Approx. $250,000	$80,000
Return Expected	8-10 times in 3 years	—	5 times in 5 yrs.	10 times in 5 yrs.	10 times in 3-5 years	5 times in 3 yrs.	5-10 times in 3-5 yrs	100%/yr. for 5 yrs.	100% in 3 years	—	50% a yr. for 3 years
Available for Investments	—	Unlimited	—	$3,000,000	—	—	—	—	$10 million	—	$500,000
Currently Invested	—	—	—	$1,000,000	—	$4,000,000	—	—	$9,000,000	$23,616,000	$80,000
People Involved	5	1	2	3	2	3	1	3	3	6	3
Profitable	75%	60%	—	20%	70%	70%	—	50%	—	—	—
Unprofitable	20%	20%	—	60%	10%	—	—	20%	—	—	—
Breakeven	5%	20%	—	20%	10%	30%	—	30%	—	—	—
Sell before Public Issue	Yes	Yes	No	No	Yes	Yes	No	Yes	—	Yes	Yes
Timing of Public Issue	4-5 years	3-5 years	2-3 years	3-5 Years	No Policy	No Policy	No Policy	2-3 Years	—	No Policy	3-5 years
Will Insert Management	Yes	No	No	Yes	No	Yes	Yes	Yes	Yes	Yes	No
Impression of Government Assistance Programs	—	Unfavourable	None	None	—	None	Unfavorable	None	Unfavorable	Unfavorable	Unfavorable
Used Government Assistance Programs	Yes S.B.A.	No	Yes	No	—	Yes S.B.A	No	No	No	Yes S.B.A.	No

CANADIAN COMPANIES - TABLE 4.1

Company	1	2	3	4	5	6	7	8	9	10	11
Started	1971	1969	1968	1969	1953	1952	1970	1963	1968	1970	1969
Will Invest In	Expansion	Start up Development expansion	Concept Start-up Development Expansion	Concept Start-up Expansion Acquisition	Expansion Turn-around Acquisition	Develop-Expansion Turn-around Acquisition	Start-up Expansion	Start-up Develop Expansion Turn-around Acquire	Start-up Development Expansion Acquire	Start-up Development Expansion	Concept Start-up
Industries Preferred	None	Electronics	None	Mining Real Estate	None	None	None	Small Industrial and Commercial	Must fit current operation	None	—
Industries Avoided	None	—	Real Estate Mining	—	High Technology	High Technology	High Technology	None	None	High technology, Real Estate	—
Other Preferences	None	High technology	Entertainment	—	—	—	Easily learn industry	None	None	None	Higher Technology
Areas Preferred	Ontario	United States Canada	None	None	Canada	Ontario Alberta B.C.	Ontario U.S.	Canada	Canada	None	Canada England
Areas Avoided	Other than Canada	None	None	South & Central America	—	None	If not readily accessible	None	Outside of Canada	Easily accessible by air	None
Range of Investments	$250,000-$500,000	$100,000-$250,000	—	$20,000-1,000,000	$20,000-1,000,000	$50,000-over 1,000,000	$50,000-500,000	$150,000 plus 75,000 shares	$50,000-1,000,000	$50,000-250,000	$5-10,000 100-250,000 500-1,000,000
Investments Made in Range	3	—	—	10	—	26	—	One acquisition	—	—	1 1 1
Maximum Investment Considered	$500,000	$250,000-$300,000	$1 million	—	$5,000,000	$1,000,000	$500,000	—	—	$250,000	—
Form of Investing	Debentures Convertible Debentures Warrants	Convertible Debentures	Mainly equity	Equity + debt+convertibles, options warrants,	Equity + debt+convertibles options warrants	Equity + debt+convertibles, options warrants	Equity	Equity plus debt	Various forms and combinations of equity and debt	Various forms and combinations of equity and debt	Equity plus debt
Equity Preferred	Minority Interest	Controlling interest	Minority interest	Control not necessary	No controlling interest	15-30%	Control not necessary	Control	Control not necessary	Control not necessary	Require control
Provide Management Services	Yes	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes	Limited	Yes
Charge for Services	None	Yes -varies	Yes -fee basis	No	Yes fee basis	Yes fee basis	Yes fee basis	Yes fee basis	No	No	Yes
Current Investments	3	2	29	—	5 private companies	50	2	1	—	8	4
Average Investment	$300,000	—	$500,000	—	$200,000	$350,000	—	$200,000	—	—	$ 150,000
Return Expected	25% compounded annually	10 times in 5 years	—	—	3 times in 5 year	15% per annum	As much as possible	—	No set policy	2 times in 2 years	60% compounded
Available for Investments	Unlimited amount for good deals	—	$7 million	#3 million	—	$18 million	$500,000	—	Unlimited	$1 million	—
Currently Invested	$900,000	—	$6.4 million	—	—	$17.5 million	—	$200,000	—	$300,000	Almost completely invested
People Involved	2	1½	3	1	4	5	1	3	1	2	3
Profitable	----	33%	70%	—	70%	60%	—	—	—	—	—
Unprofitable	----	33%	30%	—	15%	20%	—	—	—	—	—
Breakeven	----	33%	—	—	15%	20%	—	—	—	—	—
Sell Before Public Issue	----	—	—	Yes	No	Yes	No	—	Yes	No	Yes
Timing of Public Issue	As soon as possible	—	—	5 years	3-5 year	3-5 years	—	—	No set policy	3 years	—
Will Insert Management	Yes	No	Yes	—	Occasionally	No	Would consider	Yes	No	Yes	Yes
Impression of Government Assistance Programs	None	Unfavorable	—	None	Favorable	Favorable	None	Favorable	None	None	Highly Favorable
Used Government Assistance Programs	No	No	Yes	Yes O.D.C.	No	Yes P.A.I.T., I.R.D.I.A I.R.A.P. G.A.A.P.	No	Yes	None	None	Yes P.A.I.T. I.R.D.I.A. O.D.C. I.E.L. [illegible]

Company	12	13	14	15	16	17	18	19	20	01	22
Started	1969	1970	1971	1962	1968	1959	1953	1969	1963	1969	1970
Will Invest In	Concept Start-up Develop-ment	Concept Start-up Develop Expansion Acquire	Develop-ment Expansion Turn-around	Concept Start-up Develop Expansion Acquire	Concept Start-up Develop-ment Turn-around	Concept Start-up	Develop-ment Expansion Turn-around	Concept start-up Develop-ment	Concept Start-up Develop-ment Ex. Turn-around	Concept Start-up Develop-ment Expansion	Concept Start-up Acquisi-tion
Industries Preferred	———	Service Real Estate	Furniture Fabrica-ting	None	None	None	None	Growth	None	None	None
Industries Avoided	Real Estate	High Technology	———	None	None	Real Estate Merchand.	Real Es-tate.Nat. Resources	None	Real Estate Tourist	Involving high tech-nology	None
Other Preferences	High Technology	———	———	None	None	None	None	High Technology	High Technology	If familiar	None
Areas Preferred	None	North America	Ontario	None	Ontario	Ontario Br. Colum-bia	North America	None	Canada	North America	None
Areas Avoided	Must be easily accessible	None	None	None	Possibly Quebec	None	None	Quebec	None	All other than North America	None
Range of Investments	$5,000-1,000,000	$10-20,000 20-50,000 50-100,000 100-250,000	$ 5,000 - 10,000 20,000 - 50,000	$100,000 -over 1,000,000	$20-50,000 50-100,000 100,000-250,000 250,000-500,000	$100,000-1,000,000	$100,000-1,000,000	$5,000-1,000,000	$8,000-700,000	$100,000-250,000	$10-20,000 100-250,000 250-500,000
Investments Made in Range	6	2 1 2 1	1 2	———	1 3 4 2	———	———	10	———	———	2 1 2
Maximum Investment Considered	$1.5 million	$250,000	$250,000	$200,000	$2 million	$1 million	$1 million	$900,000	$1 million	$250,000	No limit
Form of Investing	Equity	Common Conver-tible Deben-tures	Common Conver-tible Preferred Options	Common Conver-tible Deben-tures Warrants	Equity Conver-tibile Debs&Pref Warrants	Equity or Equity Equiva-lent	Equity Plus Debt	Equity Plus Debt	Various forms and combina-tions of equity and debt	Combina-tion of equity and debt	Equity Conver-tible Debs. Warrants
Equity Preferred	Management not be in control	Require Control	Depends on the situation	Does not require control	10% - 40%	Less than 50%	20% - 40%	Prefer Control	Does not require control	Minority position	May require control
Provide Manage-ment Services	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes if necessary	———
Charge for Services	Yes-fee and equity basis	Yes-fee basis	Yes - variable	Yes nominal	No	Yes-fee basis	Yes-fee basis*	No	Yes-flat fee	No	———
Current Investments	6	6	———	3	8	———	23	8	20	17	———
Average Investment	———	$100,000	———	$250,000	$160,000	———	$300,000	$200,000	———	———	———
Return Expected	10 times in 7 years	———	5-10 times in 4-7 years	100% in 2 years	———	———	24 times in 4 yrs.	25% com-pounded	4-5 times in 4-5 years	4 times in 5 years	———
Available for Investments	$1,000,000	———	———	No limit	———	———	$13 million	$2.6 million	Unlimited for good deals	$2,450,000	———
Currently Invested	$150,000	———	———	———	$1,341,000	———	$5.5 million	$2.1 million	———	$2,000,000	———
People Involved	3	4	4	2	2	1	5	2	6	4	2
Profitable	———	———	———	70%	40%	———	———	75%	———	40%	———
Unprofitable	———	———	———	10%	50%	———	———	15%	———	40%	———
Breakeven	———	———	———	20%	10%	———	———	10%	———	20%	———
Sell Before Public Issue	No	Yes	———	Yes	No	Yes	———	No	Yes	No	No
Timing of Public Issue	5-7 years	———	4 years	No rule	2-5 years	———	7 years	3-5 years	7-10 years	3-5 years	2 Years
Will Insert Management	Yes	Some-times	———	No	Yes	Yes	Yes	Yes	Yes	No	No
Impression of Government Assistance Programs	———	———	———	Extremely unfavour-able	Unfav-ourable	———	Favour-able for intended objec-tives	Unfav-ourable	Favour-able	Unfav-ourable	———
Used Government Assistance Programs	———	———	———	Yes P.A.I.T., O.D.C.	No	———	Yes	No	Yes P.A.I.T.	Yes I.R.D.I.A. D.R.E.E. Manitoba Develop-	———

Company	23	24	25	26	27	28	29	30	31	32	33
Started	———	1970	1968	1968	———	1966	1967	1969	1956	1969	1965
Will Invest In	Development Expansion	Development, Expansion, Turnaround, Acquisition.	Concept Start-up Develop Expansion Acquire	Development	Concept Development Acquisitions	Any Stage	Concept	Expansion Acquisition	Acquisitions	Start up Development	Expansion
Industries Preferred	Real Estate Financial Institutions	None	Natural Resources Manufacturing	Transport Ntl. resources Financial Services	Must have some familiarity and expertise	None	None	———	Financial	None	None
Industries Avoided	Manufacturing	None	None	None	None	If require high $ amount	None	None	None	None	None
Other Preferences	No high Technology	High Technology	None	None	None	None	None	Technology	None	None	None
Areas Preferred	Canada, west coast of U.S.	United States	None	Canada	Quebec, Canada	Ontario, Quebec, N. East U.S.	None	Canada Unitied States	None	None	Ontario, Br. Columbia West U.S.
Areas Avoided	None	Canada	Political/ Economic Unstable	None	None	None	None	None	None	None	None
Range of Investments	$500,000-1,000,000	———	$20,000-500,000	$50,000-100,000 100,000-250,000 over 1,000,000	$20,000-500,000	$5-10,000 10-20,000 20-50,000 50-100,000	$5,000-250,000	$100,000-500,000	$5,000-1,000,000	$100,000-250,000 over 1,000,000	$100-250,000 250-500,000 500-1,000,000 over 1,000,000
Investments Made in Range	2	———	———	2 4 1	———	4 2 1 1	30	———	———	1 2	2 3 3 1
Maximum Investment Considered	$500,000-depends on industry	$500,000	$700,000-800,000	$4,000,000	$250,000 500,000	$100,000	$100,000	$500,000	$5-10,000,000	$1,000,000	No limit
Form of Investing	Equity and as much debt as possible	Various forms and combinations of equity and debt	Various forms and combinations of equity and debt	Secured junior debt with equity participation	Maximum equity	Combination of debt and equity	Various forms and combinations of equity and debt	Common Convertible Debentures Preferred	Common Convertible Debenture	Common, Convertible Debenture	Convertible Debenture
Equity Preferred	———	Minority Position	Generally minority positions	Minority position	Usually a minority position	50% don't require control	Do not require control	Do not require control	Do not require control	———	Less than 10%
Provide Management Services	———	No	Yes	Yes	Yes	Yes	Yes	No	Yes	———	Yes
Charge for Services	———	No	Yes, flat fee	Occasionally	Yes, variable charge	Yes, variable charge	Occasionally	No	Yes	———	No
Current Investments	2	12	———	6	———	3	30	9	20	———	———
Average Investment	———	$200,000	$300,000	$300,000	———	$20,000	———	———	———	$250,000	$500,000
Return Expected	2 times in 1-2 years	No set policy	No set policy	No set policy	No set policy	2 times in 2 years	No set policy	No set policy	———	———	3 times in 5 years
Available for Investments	———	———	———	———	———	$260,000	———	$3.5 million	$3.5 million currently available	———	$5,000,000
Currently Invested	———	———	———	———	———	$60,000	———	$3 million	———	All	———
People Involved	3	———	4	1 1/2	6	5	2	3	4	———	2
Profitable	50%	———	———	90%	———	100%	———	———	50%	———	40%
Unprofitable	15%	———	———	10%	———	———	———	———	25%	———	40%
Breakeven	35%	———	———	———	———	———	———	———	25%	———	10%
Sell Before Public Issue	Yes	No	No	No	Yes	No	No	No	No	———	Yes
Timing of Public Issue	2 years	As soon as possible	5-7 years	3-5 years	5 years	No set policy	No set policy	3 years	———	———	———
Will Insert Management	———	Yes	Seldom	No	Yes	Yes	No	No	No	———	No
Impression of Government Assistance Programs	None	Unfavourable	None	Favours only Manufacturing	None	None	None	None	Unfavourable	Unfavourable	Unfavourable
Used Government Assistance Programs	———	None	Yes O.D.C. D.R.E.E. Q.I.C.B. G.A.A.P.	None	Yes, P.A.I.T., D.R.E.E.	———	———	———	No	No	No

Company	34	35	36	37	38	39	40	41	42	43	44
Started	1965	1960	1966	1970	1970	1969	1969	1965	1969	1969	
Will Invest In	Start-up Development Acquisition Expansion	Start-up Development Expansion	Acquisition	Concept Start-up Development Expansion	Concept Start-up	Start up Development Expansion	Development Expansion Acquisition	Development Expansion	Start-up and Development	Start up Expansion	Expansion
Industries Preferred	None	None	None	High Tech. Pollution Manufacturing	None	None	None	None	None	None	None
Industries Avoided	None	None	None	Merchand. Tourist Industry	None -	None	None	None	None	None	None
Other Preferences	High Tech.	None	Metal Stamping	High Tech. Involvement	—	High technology	None	None	None	None	high growth potential
Areas Preferred	None	United States Canada	Ontario	None	Ontario	None	None	Canada	Montreal Toronto	300 miles radius of Montreal	Quebec
Areas Avoided	None	None	No	No	East coast of Canada	None	None	<10% outside Canada permitted	None	None	None
Range of Investments	$250,000-1.5 million	$50,000-175,000	$10,000-1 million	$50,000 500,000	$100,000-500,000	—	$250,000 - 5 million	$70,000-1 million	$5,000-25,000	$75,000-300,000	$20-50,000 50-100,000 100-250,000
Investments Made in Range	—	—	—	—	2	—	—	1 @ 70,000 1 & 1 million	1 @ 5,000 1 @ 22,000 1 @ 25,000	one at each level	4 2 1
Maximum Investment Considered	No limit	$175,000	$500,000	No limit	—	Will syndicate	$ 10 million	$ 1 million	Only $10,000 available	Only $70,000 left to invest	Indefinite
Form of Investing	Combination of equity and debt	Equity	Equity	Combination of equity, convertible debt option	Equity	Equity & warrants	Open	Prefer income bearing, debt or preferred, warrants	Debt & warrants	Income bearing and stock	Con. deb. warrants options
Equity Preferred	Do not require control	Do not require control	Require control	Require control	No control	Prefer Initial control	60-100%	Any, 23% & 13% in past	2-40% in past	25-55% currently	10-30% (legal man 30%)
Provide Management Services	Yes	—	Yes	Yes	Yes	Yes	Yes for short time	Yes many	Yes	Yes, heavy involved, in all services	Yes
Charge for Services	Yes	—	Yes variable	No	Yes fee	Yes	No	No	Yes, cash or equity	Yes	No
Current Investments	20	6	5	2	3	8	3	2	3	2	7
Average Investment	—	$100,000	$250,000	$200,000	$100,000	$500,000	$500,000	$500,000	$18,000	$180,000	
Return Expected	10% annually	20% annually	10% annually	25% compounded annually	2 times	—	30% compounded	—	5 times in 2 years	Large	15-20% for 5 years
Available for Investments	—	$1.1 million	—	$ 2 million	—		—	Part of large pool	$62,000	$70,000	50 million indef.amt. for ventures
Currently Invested	—	$700,000	—	—	All available	—	—	$1,070,000	$52,000	$375,000	$400,000 in ventures
People Involved	5	2	8	5	2	3	1	Part time from portfolio	1	1	3
Profitable	85%	25%	80%	—	33%	—	—	1 (large)	—	—	40%
Unprofitable	15%	25%	20%	—	33%	—	—	1 (small) written off	—	—	10%
Breakeven	—	50%	—	—	34%	—	—	—	—	—	50%
Sell before Public Issue	No	No	—	No	No	Yes	No	No	No	No	Yes
Timing of Public Issue	3-5 years	2 years	—	—	—	7 years	5 years	—	2 years	—	3-5 years
Will Insert Management	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes, heavily involved in manag.	No
Impression of Government Assistance Programs	Unfavourable	Unfavourable	Excellent	Excellent	Favourable	—	Unfamiliar	Reasonably familiar	Unfamiliar	Unfamiliar	—
Used Government Assistance Programs	Yes	Yes P.A.I.T. D.R.E.E.	Yes A.A.A.	Yes O.D.C. P.A.I.T. I.R.D.I.A. Export Dev.	Yes P.A.I.T.	—	None	None	None	None	—

TABLE 2 (continued)

Company	45	46	47	48	49	50
Started	1972(late)	1972(late)		1972(late)	1972(late)	early 1973
Will invest in	any stage depends on profitability	start-up development expansion	development	start-up development	any stage if opportunities exist	expansion turnaround acquisitions
Industries Preferred	Telecommunications	oil & gas	food agriculture oil service	high technology	secondary industry	none
Industries Avoided	--	--	--	--	--	none
Other Preferences	--	--	--	small, high technology, young		--
Areas Preferred	None	Alberta/ B.C.	Ontario, U.S. West Coast, Germany	B.C.	B.C. Alberta	Canada
Areas Avoided	low market potential	Outside Alberta/ B.C.	No underdeveloped countries	Outside B.C.	Outside west Canada	Outside Canada & U.S.
Range of Investments	-	250K-500K	10-20K 20-50K 50-100K 100-250K 250-500K	none yet	none yet, entire range	50,000-100,000 100,000-250,000 250,000-500,000
Investments made in range	-	3	3 4 1 2 1	considering 20-50K	-	none yet
Maximum Investment Considered	250,000	500,000	250K-500K	50K	depends on situation	$500,000
Form of Investing	equity	common warrants options	common convertible Dept.	common convertible	common convertible	all forms, but depends on situation
Equity Preferred	Minority	Minority	Prefer minority	Minority	Minority	20-40%
Provide Management Service	Yes	No	Yes	Yes	Yes	Yes
Charge for services	No	No	Maybe	No	No	Yes
Current Investments	-	3	2	None	None	None yet
Average Investment	-	400K	100K	-	-	--
Return Expected	30% 5-8 Yrs.	high	20% Min. per yr.	-	-	3 times in 5 yrs.
Available for Investments	$5M	$4M	$1M	60K	Large	$1,000,000
Currently Invested	-	$300K	$250K	none	-	None
People Involved	3	3	6	5	1	2
Profitable	-	-	7	-	-	20%
Unprofitable	-	-	2	-	-	20-30%
Breakeven	-	-	2	-	-	50-60%
Sell before public issue	-	-	No	-	-	Yes
Timing of Public Issue	4 yrs.	3-5 years	2 Yrs.	-	6 months - 5 Years	7-10 yrs.
Will Insert Management	-	No	No	Yes	-	No.
Impression of Government Assistance Programs	good	bad	good	not small business oriented	good	Good
Used Government Assistance	Yes	No	Yes	Yes	Yes, in other areas.	Yes

TABLE 3

NUMBER OF INVESTMENTS IN VARIOUS STAGES

	Geographical Location of Supplier							
	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
CONCEPT	7	5	5	6	2	4	10	3.5
START UP	15	10.5	11	12.5	4	7.5	22	7.5
DEVELOPMENT	21	15	12	13.5	9	17	73	25
EXPANSION	47	33	29	33	18	34	141	48
TURNAROUND	15	10.5	11	12.5	4	7.5	19	6.5
ACQUISITION	36	26	20	22.5	16	30	29	9.5
TOTALS	141		88		53		294	

NOTE: TOTALS MAY NOT AGREE WITH NUMBERS OF FIRMS DUE TO MULTIPLE ANSWERS, OMITTED ANSWERS, ETC.

SAMPLE SIZE: TOTAL CANADIAN = 50 OUTSIDE ONTARIO = 25
ONTARIO = 25 AMERICAN = 11

TABLE 4

STAGES IN WHICH SUPPLIERS WILL INVEST

Geographical Location of Supplier

	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Concept	19	14	12	15.3	7	12.1	0	0
Start up	23	16.9	19	24.3	4	6.9	8	25
Development	32	23.5	15	19.2	17	29.3	10	31.3
Expansion	32	23.5	16	20.5	16	27.6	8	25
Turnaround	11	8.1	6	7.6	5	8.6	3	9.4
Acquisition	19	14	10	12.8	9	15.5	3	9.4
TOTALS	136		78		58		32	

TABLE 5

INDUSTRIES PREFERRED BY SUPPLIERS

GEOGRAPHICAL LOCATION OF SUPPLIER

	TOTAL CANADA		ONTARIO		OUTSIDE ONTARIO		AMERICAN	
	#	%	#	%	#	%	#	%
NO PREFERENCE	28	42	17	52	11	32	5	31
HIGH TECHNOLOGY	16	24	8	24	8	23	10	62
MINING/NATURAL RESOURCES	5	7.4	1	3	4	12		
REAL ESTATE	3	4.4	2	6	1	3		
MANUFACTURING/COMMERCIAL	5	7.4	3	9	2	6	1	7
SERVICE	4	6	1	3	3	9		
TRANSPORTATION	1	1.4	0	0	1	3		
OTHER	5	7.4	1	3	4	12		
TOTALS	67		33		34		16	

TABLE 6

INDUSTRIES AVOIDED BY SUPPLIERS

	Total	Canada	Geographical Location of Supplier Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
None	26	56.5	12	48.0	14	66.6	4	67
Real Estate	6	13.2	4	16.0	2	9.6		
Mining/Natural Resources	2	4.4	2	8	0	0		
High Technology	6	13.2	4	16	2	9.6		
Manufacturing	1	2.2	0	0	1	4.8		
Merchandising	2	4.4	2	8	0	0		
Other	3	6.6	1	4	2	9.6	2	33
TOTALS	46		25		21		6	

TABLE 7

GEOGRAPHICAL AREAS PREFERRED BY SUPPLIERS

	TOTAL CANADA		GEOGRAPHICAL LOCATION OF SUPPLIER ONTARIO		OUTSIDE ONTARIO		AMERICAN	
	#	%	#	%	#	%	#	%
B.C.	6	9.4	2	6.2	4	12.6		
PRAIRIES	3	4.7	1	3.1	2	6.3		
ONTARIO	13	20.3	9	28.1	4	12.6		
QUEBEC	5	7.8	1	3.1	4	12.6		
MARITIMES	0	0	0	0	0	0		
U.S.	4	6.3	2	6.2	2	6.3	4	40
CANADA	7	10.9	4	12.4	3	9.4		
NORTH AMERICA	7	10.9	3	9.3	4	12.6	3	30
NO PREFERENCE	16	25	9	28.1	7	21.9	2	20
OTHER	3	4.7	1	3.1	2	6.3	1	10
TOTALS	64		32		32		10	

TABLE 8

GEOGRAPHICAL AREAS AVOIDED BY SUPPLIERS

	Geographical Location of Supplier							
	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
None	29	61.7	16	66.6	13	56.5	4	36.4
Outside Canada	2	4.2	2	8.3	0	0		
Not easily accessible	6	12.6	2	8.3	4	17.4	7	63.6
Quebec/Maritimes	3	6.4	3	12.5	0	0		
Outside North America	2	4.2	1	4.2	1	4.3		
Canada	1	2.1	0	0	1	4.3		
Other	4	8.4	0	0	4	17.4		
TOTALS	47		24		23		11	

TABLE 9

RANGE OF INVESTMENTS($000)

	Geographical Location of Supplier							
	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
5-10	9	6	4	4.7	5	7.7		
11-20	12	8	5	5.8	7	10.8	2	6.9
21-50	17	11.3	8	9.4	9	13.8	6	20.7
51-100	24	16	12	14.2	12	18.5	7	24.1
101-250	35	23.3	21	24.7	14	21.5	7	24.1
251-500	27	18	18	21.1	9	13.8	5	17.2
501-1000	18	12	12	14.1	6	9.2	2	6.9
>1000	8	5.3	5	5.8	3	4.6		
TOTALS	150		85		65		29	

TABLE 10

NUMBER OF INVESTMENTS IN RANGE ($000)

GEOGRAPHICAL LOCATION OF SUPPLIER

	TOTAL	CANADA	ONTARIO		OUTSIDE	ONTARIO	AMERICAN			
	#		#		#		#			
5 - 10	7		2		5					
11 - 20	9		4		5		1			
21 - 50	15		4		11		4			
51 - 100	13	30*	6	30	7		5	150	45	
101 - 250	18		10		8		15			61
251 - 500	16	52	7	52	9		13			
501 - 1000	7		1		6					
> 1000	4		2		2					
TOTALS	141		88		53		294			

* NUMBER OF INVESTMENTS MADE IN RANGE ENCLOSED BY BRACKETS.

TABLE 11

MAXIMUM INVESTMENT CONSIDERED ($000)

	Total Canada		Geographical Location of Supplier					
			Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
WILL SYNDICATE	1	2.4	0	0	1	4.8		
< 200	4	9.8	2	10	2	9.6		
200 - 500	16	39	6	30	10	47.6	6	66.6
501 - 1000	9	22	6	30	3	14.4	2	22.2
> 1000	11	26.8	6	30	5	23.8	1	11.1
TOTALS	41		20		21		9	

TABLE 12

FORM OF INVESTMENT PREFERRED BY SUPPLIERS

	Total Canada		Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Debentures	23	22.1	11	18.6	12	26.7	6	24
Convertible Debentures	20	19.2	13	22	7	15.6	5	20
Warrants	12	11.5	7	11.8	5	11.1	3	12
Equity	40	38.4	23	38.9	17	37.8	9	36
Options	7	6.7	5	8.4	2	4.4	2	8
Other	2	1.9	0	0	2	4.4	0	0
TOTALS	104		59		45		25	

TABLE 13

AMOUNT OF EQUITY PREFERRED BY SUPPLIERS

	Total Canada		Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Minority	36	76.6	16	66.7	20	87	8	72.7
Controlling	10	21.3	7	29.2	3	13	3	27.3
Depends	1	2.1	1	4.2	0	0	0	
TOTALS	47		24		23		11	

TABLE 14

PROVIDE MANAGEMENT SERVICE

			Geographical Location of Supplier					
	Total	Canada	Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Yes	39	86.7	22	95.7	17	77.3	10	91
No	4	4.4	1	4.3	3	13.6	1	9
Maybe	2	8.8	0	0	2	9.1	0	0
TOTALS	45		23		22		11	

TABLE 15

CHARGE FOR SERVICE

	Total	Canada	Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Yes	32	69.6	17	73.9	15	65.2	4	40
No	14	30.4	6	26.1	8	34.8	6	60
TOTALS	46		23		23		10	

TABLE 16

NUMBER OF CURRENT INVESTMENTS

	Total	Canada	Geographical Location of Supplier					
			Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
0 - 5	18	48.6	11	57.8	7	38.9	5	50
6 - 10	10	27	4	21	6	33.3		
11 - 20	5	13.5	1	5.2	4	22.2	3	30
21 - 30	3	8.1	2	10.4	1	5.6	1	10
> 30	1	2.7	1	5.2	0	0	1	10
TOTALS	37		19		18		10	

TABLE 17

AVERAGE SIZE OF INVESTMENT ($000)

	Geographical Location of Supplier							
	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
0 - 100	5	18.5	2	12.5	3	27.3	4	40
101 - 200	9	33.3	7	43.7	2	18.2	2	20
201 - 300	6	22.2	5	31.2	1	9.1	4	40
301 - 400	2	7.4	1	6.2	1	9.1		
> 400	5	18.5	1	6.2	4	36.4		
TOTALS	27		16		11		10	

TABLE 18

AMOUNT AVAILABLE FOR INVESTMENT ($000,000)

	Total Canada		Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
< 1	7	25.9	2	16.6	5	33.3	1	33.3
1 - 3	6	22.2	4	33.2	2	13.3	1	33.3
3 - 5	5	18.5	0	0	5	33.3		
5 - 10	1	3.7	1	8.3	0		1	33.3
10 - 20	2	7.4	2	16.6	0			
> 20	6	22.6	3	25.	3	20.		
TOTALS	27		12		15		3	

TABLE 19

AMOUNT CURRENTLY INVESTED

			Geographical Location of Supplier					
	Total	Canada	Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
0 - 200($000)	4	21.1	2	22.2	2	20	1	20
201 - 500	5	26.3	1	11.1	4	40		
501 - 1000	3	15.8	1	11.1	2	20		
1 - 5($000,000)	4	21.2	2	22.2	2	20	2	40
5 - 10	2	10.6	2	22.2	0	0	1	20
> 10	1	5.3	1	11.1	0	0	1	20
TOTALS	19		9		10		5	

TABLE 20

NUMBER OF PEOPLE INVOLVED

	Total	Canada	Ontario		Outside Ontario		American	
	Geographical Location of Supplier							
	#	%	#	%	#	%	#	%
1	8	17	5	20.8	3	13	2	18.2
2	12	25.5	7	29.1	5	21.7	2	18.2
3	10	21.3	4	16.6	6	26	5	45.6
4	7	12.8	3	12.5	4	17.4	2	18.2
5	6	12.8	4	16.6	2	8.7		
5	4	10.6	1	4.2	3	13		
TOTALS	47		24		23		11	

TABLE 21

PERCENT OF INVESTMENTS PROFITABLE

	Total	Canada	Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
33%	3	15.9	2	20	1	11.1	1	
40	4	21.2	1	10	3	33.3		
50	2	10.6	0	0	2	22.2		
							2	
60	1	5.3	1	10	0	0		
70	4	21.1	3	30	1	11.1	3	
70	5	26.5	3	30	2	22.2		
TOTALS	19		10		9		6	

TABLE 22

PERCENT OF INVESTMENTS UNPROFITABLE

	Geographical Location of Supplier							
	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
10%	1	5.2	1	10	0			
10 - 20	10	52.6	5	50	5	55.5	4	80
20 - 30	3	15.8	1	10	2	22.2		
30 - 40	4	21	2	20	2	22.2		
40 - 50	1	5.2	1	10	0		1	
TOTALS	19		10		9		5	

TABLE 23

PERCENT OF INVESTMENTS BREAK EVEN

	GEOGRAPHICAL LOCATION OF SUPPLIER							
	TOTAL CANADA		ONTARIO		OUTSIDE ONTARIO		AMERICAN	
	#	%	#	%	#	%	#	%
10 - 20%	8	57.1	5	71.4	3	42.9	4	66.6
20 - 30	1	7.1	0		1	14.3	2	33.3
30 - 40	3	21.3	2	28.6	1	14.3		
40 - 50	2	14.2	0		2	28.6		
TOTALS	14		7		7		6	

TABLE 24

SELL BEFORE PUBLIC ISSUE

	Geographical Location of Supplier							
	Total Canada		Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Yes	13	35.1	7	41.2	6	30	7	70
No	24	64.9	10	58.8	14	70	3	30
Totals	37		17		20		10	

TABLE 25

TIMING OF PUBLIC ISSUE

	Total	Canada	Geographical Location of Supplier Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
ASAP	3	9.1	2	14.3	1	5.3		
3 - 5 yrs.	21	63.6	7	50	14	73.7	6	100
5 - 7	4	12.1	3	21.4	1	5.3		
7 - 10	1	3.0			1	5.3		
No Policy	4	12.1	2	14.3	2	10.6		
Totals	33		14		19		6	

TABLE 26

WILL INSERT MANAGEMENT

	Total Canada		Geographical Location of Supplier Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Yes	25	58.1	14	63.6	11	52.4	7	63.6
No	15	34.9	5	22.7	10	47.6	4	36.4
Occasionally	3	7.0	3	13.6	0		0	
Totals	43		22		21		11	

TABLE 27

IMPRESSION OF GOVERNMENT ASSISTANCE PROGRAMS

	Total Canada		Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Good	12	30.8	8	42.1	4	20	0	
Bad	13	33.3	6	31.6	7	35	5	55.6
No Comment	14	35.9	5	26.3	9	45	4	44.4
Totals	39		19		20		9	

TABLE 28

USED GOVERNMENT ASSISTANCE PROGRAMS

	Total Canada		Geographical Location of Supplier: Ontario		Outside Ontario		American	
	#	%	#	%	#	%	#	%
Yes	22	58	11	55	11	61.1	4	40
No	16	42	9	45	7	38.9	6	60
Totals	38		20		18		10	

CHAPTER II

THE USERS OF VENTURE CAPITAL IN CANADA

Introduction

This chapter summarizes a study of users of venture capital in Canada, undertaken during the fall of 1972 and spring of 1973. The objective of this phase of the study is to complement the study of the supply side. The methodology in this phase of the study was to identify users and potential users of venture capital and question them on their experience in raising such capital and, where applicable, in obtaining grants and loans from government programs. These companies were scattered across Canada and in various industries, although the emphasis was probably on high technology firms (i.e., firms which had an innovative, patentable product) as they were the most likely candidates for venture capital.

The Sample

The population of firms for this study was gathered from many sources. The first source was venture capital suppliers whom we interviewed. Many of these venture capital firms were loathe to disclose names of user firms, both in which they had and had not invested funds. They were willing to give us names only in a list which they suggested we might contact, with no information as to whether or not they had invested in them. However, many venture capital firms would not disclose any companies which they had considered. The second source of company names was firms which had obtained funds from government grant and loan programs.

Names of these companies are published in the Public Accounts of Canada and in various other government documents available to the public. In addition, we obtained from the Department of Industry, Trade and Commerce a list of names of firms which we should contact, again without knowing whether or not they had obtained funds. The third source for company names was friends and acquaintances and other contacts.

The vast majority of firms contacted had some experience with government grant and loan programs. The Tables contain results for a sample of approximately 90 of these firms. We also asked these firms for their definition of venture capital. The common reply was equity participation in the business rather than debt and equity as emphasized by venture capital suppliers. The entrepreneurs evidently did not consider debt as venture capital, especially secured debt. The other common aspect of the definitions gathered was "for starting new ventures or expanding existing but young companies". This seemed to indicate that venture capital as defined by the users was aimed more at the start-up phase than was evident in the replies of venture capital suppliers. This was also supported by the fact that most of these companies claimed that they had obtained their start-up capital from friends, acquaintances and private individuals, rather than venture capital companies. Some of these firms thought we should include public financing, that is a public issue, as venture capital, although they agreed with our definition and the fact that public financing is available only to larger new ventures and depends heavily on the economic conditions at the time.

Once we detected user companies, we sent them an enquiry asking whether they would be willing to participate in our study and detailing what our objectives were. If the firm agreed to cooperate, we sent them a questionnaire asking various questions concerning their role in venture capital. The questionnaire was similar to the supplier questionnaire pretested on several companies before actual use. It was divided into two sections, the first including questions which were easily answered, usually in numerical form and the second asked what we consider contentious or controversial questions. To discuss these questions, we had a follow-up interview with as many of these companies as possible. Examples of this type of question would be what requirements were given in a proposal for venture capital and what should be the role of government in the provision of venture capital in Canada.

Survey Results

The results of this survey are summarized in the Tables. We shall also discuss responses to interview questions which are not reported in these Tables and shall attempt to summarize the data contained therein. The company definition of venture capital confirmed our earlier definitions as we have stated. It is obvious, however, that users consider venture capital as mainly equity and primarily oriented towards start-up and young companies. The suppliers had considered venture capital more for the purpose of expansion of established companies.

Many of the users had used outside references and found them very useful in referring them to sources of capital. These references were primarily from bankers, accountants and lawyers. However, users suggested that they had been referred by other venture capitalists to those venture capitalists with whom they had eventually negotiated to obtain funds. In addition, underwriters and investment dealers were very useful in referring entrepreneurs who could not qualify for a public issue to private venture capital companies. Many of these did so without charging finder's fees. In several instances, the federal Department of Industry, Trade and Commerce had been a useful reference to private sources. Users had a very low opinion of finders who charged a 5% fee for their referral.

User Complaints

The overriding experience evident in users and potential users of venture capital is disappointment with the attitude of venture capital firms in terms of the high cost they charged for their funds and in the narrowness of the preferences which these venture capital companies exhibited. Admittedly, much of the criticism comes from firms which were refused capital on legitimate grounds. But much of the criticism was aimed at the fact that the funds were not available for their type of business or for a company as young as theirs. Another common comment was that the venture capitalists were "looking for more glamour" than their particular firm exhibited. A different complaint from users was that venture capitalists were primarily financial experts and did not have the technical background to evaluate their particular company, especially if it was oriented to high technology.

The common problem facing both venture capital supplier and user was disagreement on the value of the firm and on how much of that firm should be offered in return for a venture capital investment. This is to be expected since entrepreneurs tend to be very optimistic about the prospects for their firm whereas venture capitalists tend to be pessimistic, based on the previous history or "track record" of the firm. Much of the criticism of the high cost of funds undoubtedly results from this disagreement over the value of the firm. The venture capitalist demands a much larger share of the equity that the user thinks he should receive, and the user is unwilling to offer it.

Locating Sources

Many of the companies studied, particularly those located in areas other than Canada's three largest cities, complained that it was nearly impossible to locate sources from which venture capital is available. It was one of our earlier conclusions that venture capital companies maintained a very low profile and had informal screening mechanisms to reduce the number of companies which approached them for funds. Several of the suppliers went so far as to say that they talked to firms only which had been referred to them by personal contacts and would not talk to anyone that simply walked in the door. So it is possibly a legitimate complaint of venture capital seekers that they face great difficulty in finding and approaching a venture capital firm.

The users claimed that an intensive investigation of their company was performed before they could qualify for venture capital and in many cases the result of this investigation was the rejection of their request for venture capital. When asked if they thought management was a significant variable lacking in their firm, most of the entrepreneurs felt that venture capital companies were using that as an excuse, but users did not generally agree. It seems reasonable to presume that entrepreneurs would not admit that their firm was lacking in management. It was a common response that a proposal to obtain venture capital should obtain financial data, both historical and pro forma, the reason for the funds, an assessment for the market of the firm's product or service, description of the organization and management involved in the firm, and a company history. Most users complained that venture capitalists expected a profitable track record for the firm before they would invest.

Where funds were obtained it was seldom less than the amount requested and plans were cut back to match the funds available. A common reply from those who received insufficient funds was that capital expenditures were often financed out of working capital, so that these firms merely fell into more of a bind for working capital.

Common and preferred shares were issued most often in exchange for venture capital. Convertible debentures seemed to be the most common form of debt used; however, bonds and debentures with warrants and options to buy common or some other equity "sweetners" were often used. Other securities usually required were personal notes and mortgages even on property other than that of the business. In general, the venture capitalist wanted the entrepreneur to have used as much of his own credit and to be as heavily extended in terms of other sources of funds as possible. It was normal that as much collateral as was available should be pledged to the venture capitalist, even when common stock was the vehicle used.

Expensive Terms

The most common criticism by users was that the terms associated with the investment of funds were too expensive and too restrictive. The high rate on the debt and preferred stock in addition to the large equity holding in their firm which was required were common sources of complaints, as illustrated in Table 22. In addition, the covenants placed on the provision of such capital as outlined in the earlier section were found to be constraining the activities of the entrepreneurs. These included restriction of capital expenditures, dividends, salaries and any capital outflow from the firm, employment contracts of management, first right on future financing, and member of the Board of Directors. Control over the purse strings by the venture capitalists was not very popular amongst the entrepreneurs.

The reasons given for refusal were usually viability of the venture, uniqueness of the collateral available, which could not be used for other purposes, lack of management experience in the company and location. The viability reason usually came for start-ups or particularly young companies.

Additional reasons given for their complaints of restrictive and binding provisions included the right to acquire control if plans did not develop, having to operate under a fixed budget with no provision for contingencies, and the constant review and monitoring which the venture capital company did. The frequency of these performance conditions is illustrated by Table 23. All of the firms refused or refusing capital had such conditions proposed. Many of the entrepreneurs resented the interference of the venture capital company in the actual management of their firm. In our opinion, the typical entrepreneur is particularly independent, wants to run his own show, and does not appreciate the interference of outside parties. Many of them had refused capital from some sources as illustrated by Table 24.

The users stated that the venture capital companies provided all sorts of additional services to their firm varying from advice as necessary to required financial and marketing planning for the company (Tables 27 and 28). The latter type of consulting was done for a fee by the venture capital company or its management subsidiary. Many of the venture capital users resented this type of service, especially when they had to pay an additional amount for it.

Perhaps the most important question asked during our study was "What are the most difficult stages to try to obtain financing?" Persons responding to this question concentrated almost strictly on the initial growth period of the company from start-up to the first two years of its operation. In general, the early years of the company before a track record was established and before market penetration could be achieved were by far the most difficult in which to obtain funds. This result tends to confirm the decision reached earlier that venture capital in

Canada is available primarily for expansion of established companies rather than for start-up or initial operation. The fact that the user company does not have a history of profitable operation usually prevents it from obtaining funds not only from banks and other low risk lenders but from venture capital companies as well. The early results for a firm are seldom highly profitable so that the most of these firms cannot raise venture capital in the early years.

Many of the entrepreneurs observed that there was limited venture capital available in Canada and what was available was limited to specific geographical areas and for particular types of investment. The second most important area which we investigated for these user companies concerned their perception of their own strengths and weaknesses of these user companies. The replies to the strengths question was typically a good management team, superior product, innovative and flexible organization and overall integrated company planning. The most common weakness stated by all of these companies was in the limited capital available for growth and the difficulty of growing rapidly within the Canadian market. But the prevailing weakness stated by nearly all of these companies was their inability to raise long-term capital as required.

Government Role

The final issue addressed in the questionnaire was whether the government could have assisted them in finding sources of capital (Tables 32 and 33). It was the opinion of most of these companies that the government programs should, at the minimum, act as a referral service to private sources of capital. They do not do so currently. Users were critical of the Industrial Development Bank and its activities as a conservative bank rather than as a small business lender. Many users suggested changing the Bank Act so that the banks could provide funds to small businesses in Canada by means other than secured loans. However, the most common suggestion was that the government should serve as a "clearing house" for borrowers and lenders attempting to get together in the venture capital arena.

Additional discussion of the Tables is also in order. The user companies varied widely in terms of their size but in general their annual sales were less than five million dollars, as illustrated in Table 4. In fact, the majority of them were under about two million dollars in sales. Most of them perceive their firms as technologically based and technologically innovative, as the data shows in Tables 7 and 8.

Initial Financing

Many of the companies stated that the original capital had been provided entirely by the founders themselves, as shown in Table 10. All of the companies investigated were started with financing from individuals and small groups rather than funds provided by a venture capital firm.

About 67% of these firms, as indicated by Table 11, had approached venture capitalists for funds but few had been successful in obtaining capital. Relatively few of them could list many venture capital companies in Canada (Table 12), and it was common that firms interviewed had little or no idea where venture capital might be obtained. They did, however, have much more extensive knowledge of government programs which provide grants and loans to businesses (Tables 13 and 14). All of them were aware of and could easily list five government programs, both federal and provincial, of which they were aware. All of them had approached some of these government programs for funds. It is surprising how many of the companies stated that they had received no instructions from the potential government source of funds on what should be included in their proposal (see Table 15). Many of them had sought assistance from outside people in preparing their requests, typically from accountants, lawyers and bankers. In almost every case they had provided a written and verbal presentation in order to obtain financing. The type of information contained in these presentations was discussed earlier.

All of the companies were investigated in depth regarding the ownership and operation of their company before funds were provided. All of them were only too willing to have the potential investor investigate their operation and to assist wherever possible. Resistance was encountered in areas where the potential investor was investigating the background of the people concerned, especially where they were probing into personal areas.

Most of the companies successful in raising funds stated that, when they did receive funds, they received exactly the amount they had requested (Table 20). Relatively few received less than the amount requested. However, many stated that they had to change plans for the use of these funds even if they received the exact amount requested (Table 21). In some cases, this was because of suggestions or recommendations by the investor while in others it was because the requested amount was not sufficient to carry out their plans.

According to over 50% of the users, the terms under which the capital was provided were more expensive or more restrictive than the entrepreneurs wished in the amount of equity required or the interest charged. They claimed to be upset by some of the provisions that venture capitalists and government programs required of them before providing the capital, as evidenced by Tables 22 and 23. The majority of them had refused to accept capital in the past in cases where the terms were too expensive (Table 24).

Just about all of the users had prospective sources of capital, especially venture capital firms, refuse their requests for funds (Table 25). It was more common that their requests for government funds would be accepted. Only about 2% of our sample had been refused by government programs. The percentage of equity provided in return for the capital received varied extensively. But it was typically in the 20-30% range, as evidenced in Table 26. Most of the companies questioned had also used additional services provided by the companies which had invested in them. In many cases, they stated that this was part of the investment contract. The vast majority of the companies were not publicly owned, as illustrated by Table 29. Very few of the companies which had sought venture capital planned to go public in the near future (Table 31).

It was a common response that government could have assisted these companies to obtain venture capital. The suggested methods of assisting varied all the way from a clearing house to help borrowers and lenders get together, to government referrals to private venture capital sources. Several of the companies went so far as to say that the tax laws should be changed to entice more private capital to become available for investment in small business. They claimed that much of the government funds currently being aimed at regional development should be channeled through private firms to deserving small businesses across Canada. They were not too clear on the details for such an undertaking, but were quite impressed and enthusiastic about the prospect of organizations like the Small Business Investment Companies in the U.S. We shall elaborate on a similar proposal for Canada in Chapter V.

Conclusions and Recommendations

In general, the users had two main complaints about the availability of venture capital in Canada. The first was that venture capital was available only for a very limited number of types of investment, mainly high technology and export oriented firms. The second was that the capital which was available was much too expensive. The users felt that the venture capitalists wanted far too much for their money and users were not willing to give up nearly as much equity control or management control as venture capitalists desired. The former comment concerning expensive debt also applied to most government incentive programs. The users stated that these were available for a very limited selection of opportunities, mainly in the research and development area. They also claimed that large companies were much more eligible for these grants and loans as they were more capable of supporting such research. Small businessmen claimed they did not have the financial resources to undertake such research and development programs, especially when grants were offerred only after completion of these programs.

Other concerns expressed by the users were the limited geographical availability of venture capital in Canada, as illustrated by Table 1, and the difficulty in determining the preferences of particular firms offering venture capital. As stated earlier, many of the venture capitalists operate through referrals only and are not accessible to the entrepreneur who walks in off the street. Service companies in particular stated that neither venture capital nor government assistance was available for their particular business except for certain regional development incentives.

Many of the managers interviewed agreed that proposals submitted to obtain both venture capital and government assistance likely left much to be desired. They claim they did not have the time or resources to devote the extensive effort in the preparation of such proposals, and did agree that they could have used assistance in preparing such documents. Many of them stated bluntly that they did not really know exactly what such a proposal should contain, and did not receive explicit instructions as to the format desired by the potential investor.

In the realm of recommendations for government action in the venture capital field, the users had many suggestions. We have summarized these into the following general recommendations:

1) The government should act as a clearing house through which entrepreneurs and venture capital sources might get together. This clearing house would have available listings of venture capital firms with their preferences and terms as well as a listing of firms seeking venture capital and the characteristics of these firms. It was suggested that proposals from the venture capital user could be available for reference for potential investors.

   The creation of such an agency would decrease the cost of obtaining venture capital by the elimination of the finder's role in the process. This should result in a saving of 5% of funds obtained to most entrepreneurs seeking capital.

2) The government should provide incentives to attract more investment into small business financing in general, especially in geographical areas where venture capital is not currently available and in industries where venture capital is not available.

Many methods of doing this were suggested such as tax incentives and direct investment in venture capital by the government. But most of the users believed that the government should not put money in directly but should create incentives for more private capital, particularly institutional capital, to flow into this area of investment. One suggestion for doing this was a mechanism similar to the Small Business Investment Companies in the United States. The users felt that if both federal and provincial governments worked jointly to arrange such a program, it could attract far more capital into the area than was currently available.

3) Government should provide assistance in developing business plans and proposals to obtain capital. This could be done through various mechanisms such as courses aimed at educating the small businessman in the preparation of such proposals and in having government people assist small businessmen directly in preparing such proposals.

These were the typical suggestions made by users interviewed. They had many other suggestions such as stating that Canadian financial institutions should get more involved in the provision of venture capital. Most of the comments were actually aimed at changes to government regulations of these institutions to provide incentive to attract more capital into the area. It is notable that most of the users did not suggest that the government should invest money directly in these companies. They are much more interested in 1) government efforts to attract more private capital into the venture capital area, 2) non-financial government assistance in referrals to likely venture capital sources and 3) help in preparation of proposals. In fact, many of the users commented that in their opinion it was not the government's job to subsidize business.

It is also noteworthy that many of the users recognize the lack of certain skills on both their part and in the venture capital companies and in government programs. They claim that many of the venture capital personnel are financial people who do not really understand high technology projects and find it difficult to evaluate them. This is also true of many government programs where an innovative business faces problems in being assessed by people evaluating the potential investment. The users therefore concluded that not only users needed assistance and education in putting together such proposals, but venture capitalists and government personnel needed further training to be able to assess these proposals.

These are suggestions which we wholeheartedly support and recommend that any government involvement in venture capital should come by providing non-financial assistance and by providing incentives through which more private capital will flow into the venture capital field.

Notes on Following Tables:

1. The firms in the Venture Capital Received group are those firms which approached a Canadian venture capital firm, were evaluated in depth and received capital.
2. The firms in the Venture Capital Refused group are those firms which approached a Canadian venture capital firm, were evaluated in depth and were either refused capital or themselves refused the offer on the grounds it was too expensive.
3. The firms in the Government Loans and Grants group are those firms who had obtained government aid. Over half of these had approached a Canadian venture capital firm but had been rejected without an in-depth evaluation. Over half of them had received funds from some source other than government in return for equity. These sources included American firms, individuals and industrial firms.
4. Totals may not agree with number of firms replying due to omitted or multiple answers.

TABLE 1

GEOGRAPHICAL LOCATION OF USER

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
British Columbia	2	12.5	1	7.1	7	12.1
Prairies	2	12.5	0	0	6	10.3
Ontario	6	37.5	6	42.9	21	36.3
Toronto	5	32.5	2	14.2	13	22.4
Quebec	0	0	0	0	0	0
Montreal	1	6.2	4	28.4	4	6.9
Maritimes	0	0	1	7.1	7	12.1
Totals	16		14		58	

TABLE 2

NUMBER OF EMPLOYEES

	Venture Capital Received		Venture Capital Refused		Government Loans	
	#	%	#	%	#	%
1 - 20	4	25	6	42.9	18	32.1
21 - 50	3	18.8	2	14.3	10	17.9
51 - 80	2	12.5	2	14.3	8	14.3
81 - 150	2	12.5	4	28.6	9	16.1
> 150	5	31.3	0	0	11	19.6
Totals	16		14		56	

TABLE 3

SIZE OF MANAGEMENT TEAM

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
1,2	4	25	4	28.6	14	25
3,4	2	12.5	3	21.4	16	28.6
5,6	5	31.3	5	35.7	13	23.2
>6	5	31.3	2	14.3	13	23.2
Totals	16		14		56	

TABLE 4

SALES VOLUME OF USERS

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
< 500,000	1	7.7	4	30.8	12	24
500,000 - 1M	2	15.4	3	23.1	9	18
1M - 2M	4	30.8	5	38.5	11	22
2M - 5M	2	15.4	1	7.7	9	18
5M - 10M	2	15.4			1	2
> 10M	2	15.4			9	18
Totals	13		13		50	

TABLE 5

TYPE OF INDUSTRY

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Food	1	6.2			5	8.6
Manufacturing	8	50	8	57.4	33	56.9
Chemicals	1	6.2			6	10.3
Electronics	2	12.5	4	28.4	8	13.8
Service	3	18.8	2	14.2	4	6.9
Other	1	6.2			2	3.4
Totals	16		14		58	

TABLE 6

AGE OF COMPANY

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
1 - 5 years	3	18.8	3	21.4	17	29.8
6 - 10	5	31.3	3	21.4	11	19.3
11 - 15	1	6.3	1	7.1	8	14
16 - 20	3	18.8	4	28.6	6	10.5
> 20	4	25	3	21.4	15	26.3
Totals	16		14		57	

TABLE 7

COMPANY TECHNOLOGICALLY BASED

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	12	75	13	92.9	46	85.2
No	4	25	1	7.1	8	14.8
Totals	16		14		54	

TABLE 8

COMPANY TECHNOLOGICALLY INNOVATIVE

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	9	56.3	12	92.3	42	77.8
No	7	43.7	1	7.7	12	22.2
Totals	16		13		54	

TABLE 9

PLAN ON SEEKING CAPITAL IN THE NEAR FUTURE

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	10	62.5	9	69.2	34	59.6
No	6	37.5	4	30.8	23	40.4
Totals	16		13		57	

TABLE 10

PERCENT OF TOTAL CAPITAL PROVIDED BY FOUNDER

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
0 - 10	5	45.5	2	16.7	15	29.4
11 - 25	3	27.3	2	16.7	7	13.7
26 - 50			2	16.7	8	15.7
51 - 75	1	9.1	1	8.4	5	9.8
76 - 100	2	18.2	5	41.7	16	31.4
Totals	11		12		51	

TABLE 11

APPROACHED A VENTURE CAPITAL COMPANY

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	16	100	14	100	30	52.6
No	0	0	0	0	27	47.4
Totals	16		14		57	

TABLE 12

LIST FIVE VENTURE CAPITAL FIRMS

		Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
		#	%	#	%	#	%
0		0	0	0	0	29	50
1,2		3	18.8	2	15.4	7	12.1
3,4		4	25	4	30.8	5	8.6
5		9	56.3	7	53.8	17	29.3
	Totals	16		13		58	

TABLE 13

APPROACHED A GOVERNMENT AGENCY

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	16	100	14	100	57	100
No	0	0	0	0	0	0
Totals	16		14		57	

TABLE 14

LIST FIVE GOVERNMENTAL ASSISTANCE PROGRAMS

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
1,2	3	19.2			7	12.1
3,4	1	6.3	2	14.3	10	17.2
5	12	75	12	85.7	41	70.7
Totals	16		14		58	

TABLE 15

RECEIVED INSTRUCTION ON WHAT SHOULD BE INCLUDED IN PROPOSAL FOR FUNDS

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	11	68.7	8	61.5	37	71.2
No	5	31.3	5	38.5	15	28.8
Totals	16		13		52	

TABLE 16

RECEIVED ASSISTANCE IN PREPARING REQUEST FOR FUNDS

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	5	31.3	5	38.5	33	61.1
No	11	68.7	8	61.5	21	38.9
Totals	16		13		54	

TABLE 17

PROVIDE A WRITTEN PRESENTATION

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	13	86.7	12	92.3	46	90.2
No	2	13.3	1	7.7	5	9.8
Totals	15		13		51	

TABLE 18

COMPANY INVESTIGATED IN DEPTH

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	14	93.3	8	50	38	74.5
No	1	6.7	8	50	13	25.5
Totals	15		16		51	

TABLE 19

AWARE THAT IN DEPTH INFORMATION HAD TO BE PROVIDED

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	14	87.5	12	92.3	48	92.3
No	2	12.5	1	7.7	4	7.7
Totals	16		13		52	

TABLE 20

IF YOU RECEIVED FUNDS DID YOU RECEIVE EXACT AMOUNT, MORE OR LESS THAN REQUESTED

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
More	1	5.6	1	11.1	2	4.3
Less	3	16.7	2	22.2	13	27.7
Exact	14	77.8	6	66.7	32	68.0
Totals	18		9		47	

TABLE 21

PLANS CHANGED AS A RESULT OF AMOUNT RECEIVED

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	1	7.2	3	37.5	14	31.8
No	13	92.8	5	62.5	30	68.2
Totals	14		8		44	

TABLE 22

TERMS MORE EXPENSIVE OR RESTRICTIVE THAN YOU WISHED

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	6	42.6	6	60	23	48.9
No	8	57.4	4	40	24	51.1
Totals	14		10		47	

TABLE 23

WERE PERFORMANCE CONDITIONS ATTACHED TO THE PROVISION OF CAPITAL

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	7	53.9	8	100	34	72.3
No	6	46.1	0	0	13	27.7
Totals	13		8		47	

TABLE 24

HAVE YOU EVER REFUSED CAPITAL

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	10	71.6	8	72.7	33	67.3
No	4	28.4	3	27.3	16	32.7
Totals	14		11		49	

TABLE 25

HAVE SOURCES OF CAPITAL REFUSED YOUR REQUEST FOR FUNDS

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	10	67.7	11	84.6	33	61.1
No	5	33.3	2	15.4	21	38.9
Totals	15		13		54	

TABLE 26

PERCENT OF STOCK PROVIDED, IF REQUIRED, TO OBTAIN FINANCING

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
0 - 10	1	7.7	3	30	8	26.7
11 - 20	2	15.4	1	10	4	13.4
21 - 30	3	23.1	3	30	7	23.3
31 - 40	6	46.2	1	10	6	20
41 - 50	1	7.7	0	0	5	16.7
50	0	0	2	20	0	-
Totals	13		10		30	

TABLE 27

DO CAPITAL SUPPLIERS PROVIDE ADDITIONAL MANAGEMENT SERVICES

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	11	73.3	9	80.2	22	56.4
No	4	26.7	2	19.8	17	43.6
Totals	15		11		39	

TABLE 28

HAVE YOU USED MANAGEMENT SERVICES

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	10	71.4	2	16.7	9	24.3
No	4	28.6	10	83.3	28	75.7
Totals	14		12		37	

TABLE 29

PUBLIC COMPANY NOW ?

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	2	13.3	1	7.1	12	27.3
No	13	86.7	13	92.9	44	72.7
Totals	15		14		56	

TABLE 30

WHEN DID YOU BECOME A PUBLIC COMPANY

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
1965 - 1973	2	66.7	-	-	5	50
1955 - 1965	1	33.3	-	-	4	40
1955	-	-	-	-	1	10
Totals	3				10	

TABLE 31

CONTEMPLATE A PUBLIC OFFERING IN THE NEAR FUTURE

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	3	30	8	66.7	16	41
No	7	70	4	33.3	23	59
Totals	10		12		39	

TABLE 32

COULD GOVERNMENT OR BUSINESS HAVE ASSISTED YOU IN FINDING SOURCES OF CAPITAL

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	7	53.9	10	76.9	34	66.7
No	6	46.1	3	23.1	17	33.3
Totals	13		13		51	

TABLE 33

COULD GOVERNMENT OR BUSINESS HAVE ASSISTED YOU IN OBTAINING CAPITAL FROM CERTAIN SOURCES

	Venture Capital Received		Venture Capital Refused		Government Loans and Grants	
	#	%	#	%	#	%
Yes	8	66.7	10	90.1	29	67.4
No	4	33.3	1	9.9	14	32.6
Totals	12		11		43	

CHAPTER III

THE ROLE OF THE FINANCIAL INSTITUTIONS

Introduction

A further objective of this study was to investigate the degree to which Canadian financial institutions participate in the provision of venture capital in Canada. These institutions are banks, trust companies, mutual funds, pension funds, finance companies, mortgage companies, life insurance companies and government institutions. One could add, caisse populaires and credit unions and investment counsellors to this although they do not really provide funds for venture capital. In addition, investment dealers do play a role to some extent, although primarily as referral agents for venture capital companies. The purpose of this phase of the study was to find to what degree do the above institutions become involved in the provision of venture capital and whether there are any obstacles to their becoming further involved. These obstacles would be primarily legislative through such acts as the Bank Act, Canadian and British Insurance Companies Act, Trust Companies Act, etc.

Second Level Investors

The primary role of the major financial institutions in Canada in supplying venture capital is the provision of funds to purchase shares in venture capital companies. In this role they are second level or silent partner participants. The capital which is available from the fifty venture capital firms described earlier has been largely provided by financial institutions and by large pools of family capital. Most of this investment from financial institutions has come through the "basket clauses" which permit a small proportion of their funds to be invested in such venture capital companies which are otherwise ineligible. A prime example is the insurance companies which are limited to investing a maximum of seven percent of their portfolio in any companies which are classed as non-eligible securities by the Canadian and British Insurance Companies Act. These ineligible securities include many public companies as well as the vast majority of the venture capital companies in Canada. The only way which money other than this "basket clause" capital might enter the venture capital market is if it were invested in a mutual fund and some of the investments of this mutual fund were in venture capital investments. However, only a small proportion of any investment in the mutual fund would find its way into venture capital investments, since such firms invest only a small proportion of their portfolio in such high risk investments.

There were very few exceptions to this second level investor role and we shall consider them in their appropriate class of institution.

Banks

The Canadian banks are typical of the second level investor in that all of them have investments in one or more venture capital companies. They claim that they refer any venture capital proposals which they encounter to the particular firm or firms in which they have investments. Toronto Dominion Bank has been the most aggressive bank by undertaking investments in five or six different venture capital companies and it is also making venture capital investments directly. This was the only bank encountered which had made venture capital investments directly. The Toronto Dominion Bank attempted to set up a separate venture capital subsidiary called the TD Capital Group. But the Bank Act prevented it from owning more than fifty percent of any Canadian corporation. The intention was to have this venture capital company controlled by the Bank and to persuade other institutions to invest funds as shareholders in it. But the Inspector General of banks has vetoed any possibility of the TD Capital Group, which is now a department of the Bank, ever being spun off as a subsidiary.

The Toronto Dominion Bank has also found the Bank Act to be a handicap in its attempts to make venture capital investments directly, since it cannot own more than fifty percent of any Canadian corporation other than a trust or loan corporation, and not more than ten percent of any firm if the net worth is over five million dollars.

In addition, the banks are not allowed to own any portion whatever of a cable television company, which has been an active area for venture capital investments recently. This was a judgment of the Canadian Radio and Television Commission recently when a bank tried to invest in such a company. The banks view this judgment as discriminating against them in particular.

But the majority of the banks do not attempt to make venture capital investments directly nor have they attempted to set up a separate venture capital subsidiary. Therefore, the Bank Act is not as great a handicap for them. The question arises whether the banks would play a more active role in this activity if the provisions of Section 76 of the Bank Act did not exist. It is especially interesting to speculate whether the Bank Act would have to be changed if Canada attempts to set up organizations such as the Small Business Investment Corporations in the United States. Many of the SBIC's in the U.S. were subsidiaries of banks, and the same would be expected in Canada under a similar arrangement. But the Bank Act currently prevents banks from getting involved in such activity and would require modification similar to that currently permitting banks to invest in trust and loan corporations.

Insurance Companies

Insurance companies, like banks, are primarily second level investors, investing in venture capital companies as shareholders. Several of the insurance companies contacted had investments in venture capital companies. Some of these, however, had invested in mutual funds which were active in venture capital investments. Few insurance companies were found which invested directly in venture capital investments. Those who were active invested in private placements of established companies, typically as part of a syndicate with other institutions. Many of these syndicates were organized by venture capital firms, who performed the evaluation and monitoring function for these syndicates. Several venture capital firms were actively involved as "packagers" of proposals for such syndicates. These private placement investments by insurance companies were rare and usually fell into the "basket clause" of the Insurance Companies Act.

Except for the "basket clause" provision, the Canadian and British Insurance Companies Act prohibits insurance companies from investing in any debt issue of a corporation that is not guaranteed or fully secured or where the corporation has not either paid a dividend in each of the past five years or had earnings sufficient to permit it to pay a dividend of at least four percent of the average value of the shares. The same applies to investment in preferred or common shares of corporations. In addition, an insurance company cannot purchase more than thirty percent of the common shares of any corporation, with minor exceptions where these investments are directly related to their insurance business. These provisions are contained in Section 63 of the Canadian and British Insurance Companies Act.

Again, for the insurance companies as for banks, provisions of the Act are not seen as significant barriers to them in investing in venture capital investments. This is primarily because most insurance companies are sufficiently conservative that they do not normally make risky investments. However, many of them do have investments in venture capital companies and these investments are usually made through the "basket clause" in the ineligible securities category. It is debatable whether the insurance companies would become more involved in the venture capital picture if the "basket clause" provision was larger or if they were permitted to invest in more risky securities.

As a class of institution, the life insurance companies are probably the least likely of the institutions to become involved in the direct provision of venture capital. The regulations for insurance companies are therefore less of a handicap for them than for any of the other institutions.

A recent study by Shaw and Archibald[1] states that Canadian insurance firms will likely move more into venture capital investments in the future. However, conversations with those authors confirm that this participation will likely be via the financing of venture capital firms as second level investors rather than direct management of investments. The primary reason is that insurance companies do not have the management expertise to begin direct venture capital investments. This will be discussed further later in this chapter for all financial institutions.

Trust Companies

The trust companies, like the insurance companies, were found to be primarily second level investors and rarely became active in making direct venture capital investments. Some of them are shareholders in venture capital companies, but are not permitted

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1. D. C. Shaw and T. R. Archibald, "Management of Change in the Canadian Securities Industry - Study 4 - Life Insurance Companies in Canada", March 1973.

by the Trust Companies Act to get highly involved directly in venture capital situations. The Trust Companies Act is very similar to the Insurance Companies Act in terms of the type of investment which the trust company may make. In addition, trust companies are permitted to invest trustee funds only in such securities as are authorized by the instrument creating the trust. Typically, most trust funds do not provide for investments in venture capital situations.

It is doubtful whether the trust companies would become very active in providing venture capital other than as second level investors if the provisions of the Trust Companies Act were relaxed.

Loan Companies

The Loan Companies Act is similar to the Trust Companies Act in terms of the permissable investments which loan companies can make. It is doubtful whether loan companies would become more aggressive in terms of venture capital investments if this Act were relaxed. The remarks made about trust companies apply equally well to loan companies in Canada.

Pension Funds

Pension funds in Canada were found to be active in venture capital companies as second level investors but rarely as direct investors. Few exceptions to this were encountered. Those the pension funds which had ever been involved in making direct venture capital investments had only made a few of them and typically did not do so any longer. This is primarily because the management within the pension fund was not trained for capable evaluation of venture capital situations. Their expertise was in managing portfolios of marketable securities. Therefore, most of the pension funds quickly found they did not have the management capability to operate as a direct supplier of venture capital. This is also true of most of the institutions which we encountered during the study. However, several of the venture capital companies listed in the supplier section of this report were pension funds who have been directly involved in providing venture capital in the past. It is doubtful whether they will be highly involved in that area in the future. Several of them have recently invested in a venture capital firm created by the Canadian Development Corporation.

Pension funds had made these investments under the "basket clause" of seven percent of their portfolio, which included all ineligible securities. Relatively few of the pension funds were found who considered the seven percent restriction to be a significant obstacle in their investments. Only the more aggressive pension funds were pushing this seven percent limit, and typically because of their investments in ineligible public securities rather than in non-public companies.

However, the pension funds have exhibited the greatest growth of any of the institutions during recent years. They now hold such a large portfolio that even a small fraction of one percent of their funds directed into venture capital would overwhelm the total amount of capital available for venture capital situations currently.

It is unlikely that pension funds will become very active directly in making venture capital investments but will more likely continue in their role as second level investors. Again, a number of them have invested in mutual funds which have venture capital investments and some of these funds have been channelled indirectly into venture capital investments.

The legislation governing pension funds was not seen as a significant handicap to pension funds becoming more active in this area. However, if more funds are channelled into venture capital situations by the pension funds, the seven percent "basket clause" limit may become a problem for them. This is not because they are likely to invest seven percent of their funds in venture capital situations but because the total number of ineligible securities in which they have investments, including venture capital situations, may grow in the future. This is especially likely when one considers the trend by Canadian financial institutions to invest more actively in higher risk securities than they have in the past. In addition, the Canadian capital markets are claimed not to have sufficient depth for the institutions to buy and sell easily.[1] This causes liquidity problems and marketability problems for the institutions. These changing

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[1] "New Ground Rules Money Managers Face", Financial Post, December 10, 1972.

conditions may cause some of the financial institutions to become more active in non-liquid investments such as venture capital. If this happens, the seven percent limit may become a problem.

Mutual Funds

The most actively involved of all the institutions in the venture capital picture were the mutual funds. A number of these had investments in venture capital situations, usually through a separate fund set up for that purpose. Under this arrangement, a fraction of the total portfolio of the mutual fund was directed into a new fund for venture capital investments. This amount was typically small (less than five percent of each such fund) and not too significant considering the total portfolio of mutual funds. However, many mutual funds claimed they did not get involved in venture capital investments at all, and only a handful of the venture capital suppliers discussed earlier are mutual funds.

Other Institutions

Other companies, such as mortgage companies, finance companies and leasing companies, do not actively invest in venture capital. Some of them may be second level investors in venture capital companies, but it is unlikely that they will become actively involved in such activity. They are primarily oriented towards completely secured lending activity. Current legislation is not seen as a handicap for them since they usually have no desire to get involved in such activity.

If the institutions discussed above, particularly the pension funds, were to invest a tenth of one percent of their funds in the venture capital area, it would significantly outweigh the total funds available for venture capital investment in Canada currently. Thus any move by the government to give the institutions more incentive to invest in venture situations could result in a significant flow of funds into such investments without changes in the current institutional legislation.

<u>The Canada Development Corporation</u>

Another recent institution on the Canadian financial scene is the Canadian Development Corporation. Although currently wholly owned by the federal government, it will become a public company in the near future. It has been more influential in the provision of venture capital during its short lifetime than any of the other institutions mentioned earlier. By setting up three separate venture capital companies in different areas of Canada, it has released a significant amount of capital into the pool available for venture capital investments. Since the CDC cannot make investments under one million dollars, it is prohibited from investing directly in venture capital situations itself. It must therefore invest through venture capital companies as a second level or silent partner.

The only other institutions in the venture capital market are investment dealers and investment counsellors. Investment dealers become involved typically through referrals, whereby if a company is attempting to go public, the dealer may refer them to a venture capital company for bridge financing. This is financing to continue their operations until they are large enough or the time is right for a public issue. The investment dealer may invest some money through the venture capital company itself. But investment dealers and individuals within the investment dealer community usually become involved by investing directly into venture capital situations independently. There are many individuals in the overall financial market who do make such investments either alone or in small groups, but these groups are usually formed on an ad hoc basis for each investment and they seldom make more than a few investments. It was therefore difficult to attempt to estimate the overall availability of capital on these terms. However, investment dealers do provide a referral service and, to some degree, they do some prior screening for venture capital companies.

Investment counsellors get involved especially in referrals to venture capital companies, but some of them serve as finders and brokers of venture capital deals as well. We have discussed the finder classification earlier. Brokers are typically individuals who will attempt to help the entrepreneur assemble and complete his proposal to obtain funds and will then take the proposal to venture capital sources which he knows in an attempt to raise capital for it. Some of these brokers will put in money of their own and to that extent become packagers of venture capital as discussed earlier. But most brokers do not typically make substantial capital investment themselves. Nevertheless, they provide a very useful service to the venture capital community in the screening that they do and in the liaison which they provide between user of capital and supplier of capital.

Barriers to the Financial Institutions

Lack of Management

Possibly the greatest barrier preventing the financial institutions from investing directly in venture capital is the lack of management personnel trained to evaluate and monitor venture capital investments. Those institutions interviewed which had made direct investments usually had ceased making their own investments and were making them through a venture capital company, because of the amount of management time and effort which was required to evaluate and monitor each venture. The average venture investment is much smaller than the value of each stock held in a portfolio, but a $100,000 venture is more troublesome than a $1,000,000 volume of stock in the portfolio.

Institutional managers are experienced in analyzing the securities of public companies, but different skills are required to administer a venture capital portfolio. Institutions would have to train their management to administer venture capital investments or hire managers skilled in this activity.

Instead, firms have developed ("packagers") which specialize in the analysis and monitoring of venture investments. These firms will invest the capital of the financial institutions and manage the venture portfolio for a fee. Other institutions invest directly in venture capital companies and leave it to the venture manager's judgment to choose the investments. In the packager's approach, however, each institution can decide how much of its own capital, if any, is invested in each venture, and most ventures are joint investments among institutions and the packager.

As the intermediary function of packagers and venture capital firms becomes more sophisticated, more institutions will likely invest through them. The extreme case of this approach is the Small Business Investment Company in the U.S., which draws most of its capital from institutions, using government guaranteed debentures. If this type of intermediary function is developed in Canada, institutions will find it much easier to devote a portion of their portfolio to venture capital investments.

The Effects of Government Regulations

In general, the majority of officers in the financial institutions surveyed agreed that the current regulations under which they operate did not significantly hamper them in making investments in the venture capital area. Most of them are currently much too conservative, both because of the acts under which they operate and because of the management attitude within these companies.

There are some exceptions among the institutions as mentioned earlier. The more aggressive banks, pension funds and life insurance companies have become more active in making venture capital investments directly but not on a very large scale. The Toronto Dominion Bank is essentially the only institution encountered which is prevented by the Bank Act from entering the venture capital field to the extent which it would like. Several of the pension funds are apparently finding the seven percent basket clause limit binding because of the amount of ineligible public securities, private placements and venture capital investments which they have made, but it is not the venture capital investments alone which cause this bind. The number of such institutions is relatively limited. As mentioned, the mutual funds tend to get more involved than other institutions with venture capital subsections in many funds. But trust companies, loan companies and other financial institutions do not get involved in venture capital investment directly to any significant degree. Nearly all of the institutions surveyed, however, make investments as second level investors or silent partners in venture capital companies. This is probably the best way for them to become involved in venture capital deals because they do not have the capability to evaluate and monitor venture capital investments.

Any changes in government policy aimed at having institutions redirect more funds into venture capital areas should therefore be aimed at providing incentive to these institutions to direct a larger proportion of their total portfolio into venture capital companies as second level investors. Possible methods of doing this will be discussed later in Chapter 5.

Another common reason for the lack of institutional activity in the direct provision of venture capital was the size of the investment involved. As mentioned earlier, the average venture capital investment is in the order of $200,000 to $250,000. This is much smaller than most institutions would be willing to consider, since most of their investments are of the order of a million dollars and larger. This reason was also quoted by some venture capital companies who relied heavily on institutions when they attempted to syndicate a venture. It is obvious that the large institutional pools of capital would prefer to make relatively large investments in less risky situations than to split that investment into many smaller more risky situations.

This pressure from institutional shareholders for venture capital companies to make relatively large investments and in less risky situations is one primary reason why venture capital companies in Canada are oriented towards expansion of medium-sized established companies rather than start-up or investment in young companies.

Therefore, one must understand that the venture capitalist himself is under pressure from both sides. From the entrepreneurs, he is under pressure to invest in earlier stages of the company's history. From the institutional investors, he is under pressure to perform in the short term and to make less risky investments than he might otherwise if he controlled the funds totally himself.

The primary concern with institutional financing of venture capital, then, is how to change the total amount of funds allocated by institutions for such investment. Various incentive measures have been proposed which would re-direct more institutional capital into the venture field. These shall be discussed in the last chapter. However, various managers have suggested that there is not sufficient depth in the Canadian public securities markets to absorb the current growth of our large financial institutions. In addition, the management of financial institutions has become more aggressive as illustrated by their portfolios.[1]

It is therefore a definite possibility that the institutions will direct more of their funds towards the non-public sector, notably into investments in small companies. However, a sophisticated intermediary function must be set up to do this or the institutions must train their own venture managers. Several of these intermediaries have been formed in recent years, and were discussed earlier under the name "packagers". This is a relatively new form of intermediary, but it will play a greater role in the financing of small business in the future. More of this activity may be expected as more and more institutional capital is directed towards the more risky investments. This will be especially true if government becomes involved, providing incentives to institutions to redirect more capital into this area.

In summary, however, Canadian institutions do not currently play a major role in direct venture capital investment. They do act primarily as second level investors and may be instrumental in setting the policies under which most of the venture

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[1]This change is discussed in detail by T.R. Archibald and D.C. Shaw in "Canada's Capital Markets", published by the Toronto Stock Exchange.

capital companies operate. Thus the tendency of Canadian venture capital companies to be oriented towards expansion of medium sized companies may be attributable to the institutional investors. It is suggested that government should concentrate on providing incentives to cause more institutional capital to flow into investment in smaller companies.

CHAPTER IV

GOVERNMENT FINANCIAL INTERMEDIARIES

Introduction

The importance of government grant and loan programs in the financing of small businesses in Canada is the focus for this chapter. Both federal and provincial programs in Canada are included although most of the federal programs examined were in one department, namely the Department of Industry, Trade and Commerce. Interviews with officials in fifteen different government programs (12 federal, 3 provincial) were conducted as well as 62 interviews with users of these government programs. Some aggregate statistics were gathered on the firms to which loans and grants were awarded, but most of these programs do not publish such data.

In summary, the majority of the government programs examined apply equally to large and small companies. In fact, large companies can take better advantage of most of these programs since they usually have a favorable performance record, larger debt capacity and have the professional expertise provided by lawyers and accountants, and the resources to devote sufficient time and manpower to prepare their case for securing such grants and loans. The only program found which was aimed primarily at small business was the Industrial Development Bank. But this bank is really a very conservative lending institution, since it has provided equity in only two or three cases in its history and all its loans are fully secured. Admittedly, it is a significant source of assistance to small business, but most of its customers could obtain loans equally well on similar terms from private financial institutions such as Roynat.[1] Although the charter of the Industrial Development Bank makes provision for issuing equity and underwriting activity, the IDB has never become actively involved in this phase of small business financing. Most small businesses need equity capital, since their debt generating capacity is already exhausted. Therefore, the IDB is not considered a primary source of venture capital by our definition. All of its funds are issued as fully secured loans.

Listings of both federal and provincial government programs which were examined are contained in Appendices 1 and 2. A brief summary of each program including its purpose, form of aid provided and criteria for eligibility, is contained in the same exhibit.

Federal Programs

Availability to Small Business

The majority of the federal programs available to businesses in Canada is oriented towards research and development and apply primarily to high technology companies and large firms. Most small businesses cannot devote significant resources to research and development. For example, the Program for the Advancement of Industrial Technology is a valuable source of aid at the develop-

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1. "Do We Really Need the IDB Anymore?", The Financial Post, November 18, 1972.

mental stage for firms that qualify. However, the majority of the aid from these research and development oriented programs is directed to large firms rather than small ones. Exhibit 1 presents some statistics on the size of firm to which grants and loans have been made from several programs, including P.A.I.T.

The most significant aspect of all the federal programs is that they are primarily available only to established companies. Like the private venture capital sources, government analysts evaluate a company's past performance and, especially in the case of loans, determine its ability to repay such aid. Thus, young companies stand little chance of being awarded these loans. In general, government programs are aimed at the expansion phase rather than at the start-up or developmental phase, as was the case for venture capital from private sources.

Programs which were reported as useful to small businesses are the Counselling Assistance to Small Enterprises (CASE) which attempts to improve the management ability in small firms, (although it is limited to the Montreal and Winnipeg areas currently) the Small Business Loans Program which has the deficiency of supplying only secured debt, and the Department of Regional Economic Expansion. The latter is usually the only federal program for which many of the small businesses in the rural areas of Canada qualify, since many are service firms. The fact that it is primarily directed towards capital intensive industries (despite the objective of increasing employment) while small businesses are not capital intensive, proves to be its major weakness as a source of funds for small firms. For example, many distribution firms in the Maritime provinces require a small investment in plant and equipment, but employ large numbers of people and have large inventories. The need for working capital is therefore greater in such firms than the need for capital to purchase fixed assets. But it is not available from D.R.E.E.

Other programs which could benefit small firms are the export oriented programs such as the Program for Export Market Development and the Export Development Corporation. However, most small firms are not export oriented during the early stages of their life, and do not qualify for such aid. For those small domestic firms whose primary markets are in other countries, these programs offer substantial potential assistance. A new program which should benefit small firms in the far north is the Incentive Programs North of 60.

Most of the other programs described in Appendix 1 are specialized and only small businesses in particular industries may qualify for them, as illustrated by the eligibility criteria in Appendix 1.

In summary, the basic problem with most federal programs is that they provide loan capital only and most small businesses are already extended with debt. Even those programs which can invest in equity, such as the IDB, do not. We conclude that, in general, the federal programs are not a significant source of venture capital to small businesses.

One useful discovery was the vast amount of industrial and statistical information available to all firms from government sources regarding competition, products and markets. It is doubtful whether most firms take advantage of the government resources at their disposal and the amount of information available to them for the asking. We believe that the federal government should heavily promote this aspect of their service to small firms, and should centralize this activity by creating a department like the Small Business Administration in the United States, which specializes in providing financing and information to small business.

An important service of the Industrial Development Bank that is usually overlooked is their Advisory Services Program which helps promote improved management practices by offering courses and counselling assistance to small businesses in Canada. We believe that this activity should be expanded and this suggestion will be expanded in later sections.

Interviews with Federal Program Officials

We conducted interviews with officers from twelve different federal programs. They agreed that, while our definition of venture capital included the definition of their program, they did not consider their programs as sources of venture capital. These programs offer industrial and commercial incentives and assistance in the form of direct and forgiveable loans and grants. The officials agreed that in some cases they may be financing higher risk research, but in every instance where a loan was made, tests for financial stability in the form of a performance record and other criteria were required. The incentive grants were usually made in the form of reimbursement of validated expenses so that the receiving company had to have the actual financial strength to support the project, at least temporarily.

All of the administrators believed that their program offered its benefits primarily to larger, more established companies. They cited criteria of financial strength and performance as a key factor in the extension of program services and financial aid to those businesses. All of those interviewed acknowledged the fact that many small companies have borrowed to their limit under conventional credit terms and that their performance record, or lack of it, may not reflect their true potential. However, the administrators quickly pointed out that the programs must conform to the policy decisions or legislative acts under which they are set up. This usually restricts the amount of financing which they can make available to the small firms.

Several of the program administrators observed that the application forms were too complicated for the average businessman. These officials pointed out that many small businessmen did not have the resources in terms of management time or skill to develop the necessary relationship with the program which appears to be required for gaining such financial assistance. The administrators usually stated their role as guardians of the public funds and the information requested on the application was required to safeguard these funds. Perhaps this attitude has created the need for a group of individuals, who, for a fee, will complete a firm's application and present it for the company to program administrators. A number of these professional fund-raisers who specialize in gaining government loans and grants for businesses have established themselves, primarily in Ottawa. However, the fees which they charge make them more accessible to large than to small firms.

Government program officers usually considered venture capital as equity financing and unanimously agreed that they could not conceive of this type of financing being available under a government program because of its political implications. They also said that they did not have sufficient personnel or the necessary expertise in underwriting and managing equity securities and they considered the cost of acquiring such talent prohibitive. In the opinion of these officials, the government programs could, on the whole, achieve their objectives with the investment vehicles currently available.

These administrators countered the suggestion of SBIC program for Canada with the comment that it was not feasible and they were also skeptical of the success potential of such an agency, and expressed their doubts about its success in the United States. All agreed that an in-depth investigation would be required before deciding whether or not an SBIC program would be useful in Canada.

When asked what further services should be offered to small business by the government, all of these administrators replied in terms of "housecleaning" approaches or improvements to their own program. They spoke hopefully about expanding their own program, simplifying the administrative procedures and generally improving its functioning. They resisted forecasting what the future orientation of the government's approach to providing financial assistance would be and had no plans to suggest.

Government administrators interviewed believe that the shortage of venture capital in Canada is not as acute as suggested in the Gray Report. For worthwhile projects, they suggested there was no difficulty in obtaining funds. In their opinion, the question of financing was not the main concern for small business in Canada. They emphasized that venture management was decidedly more lacking than venture financing and pointed out that increasing the amount of funds available would not assist in significant upgrading of new Canadian businesses.

The Broker Function

One concept advanced during the interviews was that of a broker for small businessmen seeking funds. One program administrator suggested that one of the prime problems of businesses seeking financing in Canada was the large number of middlemen or finders who get involved in the procurement of such financing and compound the difficulty of finding the right source. The government's role should perhaps be in providing this unbiased broker function rather than advancing more capital. The role of this unbiased broker would be to help the small businessman find and obtain such private capital from current existing sources by assisting him in writing proposals and approaching the right sources.

This particular administrator saw a need for a function for the public service to preview or prescreen applicants with the intent of assisting them to develop a more sophisticated understanding of their own specific project. It would also be their function to direct the applicant to the appropriate sources of public and private financial assistance. This would allow proposals to be judged more openly and with a fairer assessment of the future of each project than finders currently provide. This concept would add one more step in the evaluation system of ventures, but the viewpoint of this last step would be a more sympathetic one to the innovator or entrepreneur. It might possibly result in the development of some valuable ideas which might not otherwise have been exploited by advising the entrepreneurs on the proper mix of private and public financing.

Incentive Programs and Size of Firm

Exhibits 1 and 2 present information about the size of firm by sales volume for recipients of aid from several programs in the Department of Industry, Trade and Commerce. These figures are based on several hundred approved projects during 1971 and 1972. Approximately 50% of the aid in the PAIT program is given to firms with sales over five million dollars. Several of these government programs assist small firms but the Industrial Design

Assistance Program is essentially aid for product design and is really research and development oriented. The data in these exhibits indicate that first, a relatively small percentage of project proposals are approved and second, that the majority of those approved tend to be high-technology, directed towards chemical, electrical and machinery industries.

When asked what their program implied for small and new companies, all the government program administrators replied that they were not in the business of helping people start new businesses. They usually added that before considering a company for financing they preferred to see a five-year profit record. The data presented in the exhibits and the attitude expressed by most of the officials interviewed and described in the previous paragraphs indicate that the guidelines of these government programs are not sufficiently broad to enable them to provide substantial financial support to developing business firms.

The Industrial Development Bank

The financial assets of the Industrial Development Bank alone exceed the reported assets of the provincial and private sources of funds for small business. The resources of the Industrial Development Bank account for 59% of the assets of all federal and provincial government industrial lending institutions. Therefore, the IDB funds provided each year far outweigh other sources of funds available to small business in Canada. However, the fact that IDB funds are available only for fully secured loans limits the use of these funds to established companies in general. It also limits these funds to companies which have capital assets available as security.

Selected statistics for the Industrial Development Bank are shown in Exhibits 3 through 5. Approximately half by number of their loans are for $25,000 or less, and approximately half of these is advanced for the purchase of land and buildings. A declining share has been allocated to manufacturing firms, amounting to 22% of the total in 1972 compared to 29% in 1968. Sixty-two percent of the loans made by the IDB were made to service industries in 1972, with 16% unspecified by industry. This is one of the few sources of funds which seems to specialize in service industries. Since most businesses in Canada are of the service type[2] this may explain the preponderance of service company loans by the IDB.

We concluded earlier in this paper that the IDB was not a significant source of venture capital. We believe that the IDB is not serving the function which was intended for it in its original charter, but has become a competitor for the private lending institutions.

In addition, the IDB charges interest rates in the order of nine to ten percent and the rate increases with the size of the loan. In fact, some authors have recently questioned whether or not the IDB still serves a useful purpose.[3] In the opinion of

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2. Concentration in the Manufacturing Industries of Canada, Department of Consumer and Corporate Affairs, Ottawa, 1971, p.14.

3. The Financial Post, "Do We Really Need the IDB Anymore?", November 18, 1972.

some observers, the IDB has largely been replaced by such private institutions as Roynat and the various provincial lending agencies which have developed since the IDB was formed. With the exception of British Columbia, which had no provincial lending agency until plans for one were announced this year, IDB loans to all provinces have fallen off in the 1960s. In fact, the province whose percentage of IDB loans rose most sharply was British Columbia[4],mainly since the IDB has been the only government lending institution available to British Columbia firms. IDB loans in B.C. in 1971 amounted to over $85 million or approximately one-third of the Canadian total. In addition, the Small Business Loans Act, created in 1961, authorizes government guarantees of loans made to small businesses by the charter banks up to a maximum of $25,000. Since this size of loan makes up about half of the IDB loans, the IDB and SBLA seem to represent unnecessary duplication within this range. However, the SBLA is used far less frequently and bank managers interviewed were often not even aware of it.

The fact that the IDB is in direct competition with private lenders is often a point of contention among these private lenders who claim that the IDB is being subsidized to compete directly with them. This presumably places private lenders at a disadvantage to the IDB since the government can raise funds for the IDB at a lower cost than private institutions. We believe

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4 Source: IDB Annual Reports, 1972.

the IDB should undertake the financing that the original act intended and provide assistance to small businesses which cannot obtain financial assistance elsewhere. In this role, the IDB should adopt a more responsible risk taking posture and offer financing to small firms in the start-up and developmental stages of the life cycle. The critics suggesting this include the IDB users interviewed.

Department of Regional Economic Expansion

This department was established in 1969 to provide assistance to companies in economically depressed regions of Canada. Some of the investment of DREE funds has been made to large firms relocating or expanding into the DREE areas. An example is Michelin Tire Company, currently producing tires in Nova Scotia. One of the objectives of DREE is to provide jobs and therefore one might expect allocations to be directed towards labor intensive industry; but its grants are available primarily for capital intensive industry. This tends to create a conflictive of objectives within DREE. It also favors companies building large plants rather than the small service oriented industries existing in these areas of Canada. The distribution companies in the Maritime provinces described previously operate with low fixed assets but fairly large inventories and a need for working capital. These firms are typically not eligible for DREE funds. In fact, service industries cannot obtain DREE grants for expansion or modernization, but manufacturing and processing industries can.

In addition to incentive grants, DREE can provide loan guarantees, but this activity is considerably less important than the incentive grant area as illustrated in Exhibits 6 and 7. These exhibits show the number of applications under each classification and the total amount of funds supplied to the end of 1972. No figures were available on DREE financing by size of firm or by type of industry. Exhibit 8 on the Area Incentive Act of DREE illustrates that the average investment in fixed assets per application is larger than most small businesses could make. The average grant for the active cases as of the end of March 1970 was $1.7 million and the average tax incentive sought was $2.7 million. These figures are obviously larger than most small businesses could support. Therefore we conclude that many of the DREE incentive grants are not available for small business firms.

The provisions for DREE grants state that incentive grants are available to manufacturing and processing industries only, and not to certain natural resource processing industries. Service industries are eligible for loan guarantees and service firms applying for these must be new firms, not existing companies, expanding or modernizing their facilities. Manufacturing and processing firms can apply for incentive grants for expansion or modernization as well as for new facilities.

From interviews with users of government funds, however, we concluded that for many of the firms in the Maritime and Prairie provinces, DREE is about the only source of financing available. These users consider that government sources of funds such as DREE are venture capital, although they complained that DREE grants and government grants in general are much more available to large companies than to small firms.

Provincial Assistance Programs

The main provincial industrial assistance programs are outlined in Appendix 2, along with the purpose of each program and the main criteria for eligibility. Most of the provinces have an industrial development program similar to the Ontario Development Corporation (ODC). We shall concentrate on the ODC in this evaluation, but many of the comments apply equally well to other provincial intermediaries.

As mentioned earlier, the provincial lending institutions are collectively smaller than the IDB. The largest provincial program is Industrial Estates Limited of Nova Scotia which is approximately one-fifth the size of the IDB. IEL is about twice as large as the Manitoba Development Corporation and Quebec's General Investment Corporation. The Ontario Development Corporation is in turn only about one-fifth the size of Manitoba and Quebec funds and thus one-tenth the size of IEL or one-fiftieth the size of the IDB. The other provincial funds make up a smaller proportion of the total.

Provincial industrial assistance programs, like the federal programs discussed earlier, generally do not provide equity financing. They supply secured term loans or, in some cases, forgiveable loans as we have continually pointed out. The typical small business often cannot afford an increased debt load. We encountered a number of firms which had obtained funds from provincial agencies, but which had paid them off because they found them too expensive to maintain in terms of the interest payments required. In addition, most of the provincial government programs require as much security as possible for loans, and often require deferral by all other creditors. These terms have caused potential users to refuse the loans after they had been approved. These provincial financial institutions are usually very oriented towards maximum security in their investments, like the IDB, and often tend to make investments in large companies in preference to small ones.

An illustration of conservatism of these programs is provided by the Manitoba Development Corporation, which had no losses reported prior to 1967. During the period from 1958 to 1967, it had approved about 730 loans for a total investment of over 52 million dollars. This gives some indication that the loans were not in high risk investments. On the other hand, the Ontario Development Corporation does seem to be more aggressive, as evidenced by a bad debt provision of 13 percent in 1967 and 6 percent in 1968. The total assets of the ODC were about $8 million in 1970 as compared to approximately $40 million for the Manitoba Development Corporation. The ODC can purchase equity as well as issue loans, but has rarely done so up to now.

The practices of the provincial industrial assistance programs seem inconsistent with their stated objectives. Their requirements are usually too restrictive to benefit most small firms, especially at the start-up and development phase.

We disagree with one critic who characterized the ODC as being the most inefficient of the provincial financial assistance programs because of its bad debt losses.[5] We conclude that the ODC is more aggressive than other provincial institutions and supports higher risk investments. A recent addition to the ODC is a program called Venture Capital for Canadians. One of the stated objectives of the ODC is to provide venture capital to businesses in Ontario. Our criticism with the ODC is that it offers primarily loans to small businesses even within this new program. It has seldom acquired equity in the past, and therefore failed to meet our definition of a venture capital supplier.

Interviews with Users of Government Programs

Many of the firms included as users of venture capital in Chapter 2 had also received funds from government programs. The mail questionnaire and interviews captured some of their thoughts regarding these programs. We interviewed a sample of sixty-two firms which had used various government programs. Fifty-nine firms had used one or more federal government programs while three used only provincial programs. Twelve of the users of federal programs had also used various provincial programs. The

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5. E. J. Doak, Financial Intermediation by Government, Unpublished Ph.D. Thesis, University of Toronto, 1970.

breakdown in terms of programs used were: PAIT - 11, DREE - 7, IDB - 9, other federal programs - 20, combination of federal and provincial programs - 12, provincial only - 3.

Approximately 80 percent of the firms interviewed were not publicly held companies and those which were public had typically gone public during the late 1960s, or early 1970s. About 40 percent of those which were not public contemplated a public offering in the next three to five years.

Over 75% of these firms were aware of at least five government assistance programs at both the federal and provincial level, as illustrated in Table 14 of the previous chapter. This was a much higher awareness level than expressed for venture capital firms, possibly because the governmental firms advertise extensively and distribute literature on their programs, unlike venture capital firms. Many of these user firms replied that they have received less funds than they had requested, primarily because they did not have sufficient collateral to secure the full amount. In most of these cases, their plans for the use of these funds were changed considerably as a result of the amount obtained.

In addition, approximately 85 percent of the firms interviewed had prospective sources of capital refuse their requests for funds. Most of these had been private sources of capital, but many of them had been refused by government programs as well. This refusal was usually on the grounds that they did not qualify for the particular program for which they had applied, rather than rejections after their applications had been completed.

The terms under which the funds were provided were often more expensive and restrictive than the firms thought was reasonable. When enquiring more deeply into this issue, we found that the interest rates were usually as high or higher than for private sources and the limitations on the uses of the capital obtained were usually as strict as imposed by private sources. More users complained that the conditions were too strict than complained about the cost. Nearly 90% of these firms had at some time refused funds because of the cost and the restrictions. In over half of these cases, we found that capital had been refused from a government grant on the grounds that it was too expensive.

These firms also replied overwhelmingly as illustrated in Table 32 of Chapter III that government could have assisted them in finding other sources of capital in addition to the government program for which they applied and obtaining these funds. Feedback on their government proposals and assistance in approaching the source more likely to supply funds to their type of company were cited as particular benefits.

Complaints About Government Programs

By far the most common complaint about the various government programs was that these programs were available only for a very limited number and type of companies such as those heavily engaged in research and development. Many of the small firms interviewed, particularly those in service industries, stated that there was no government program which offered aid to them.

This was especially true of service companies which did not qualify for any of the regional expansion programs; however, even service companies in areas designated for government incentive assistance did not typically qualify, since most of the government aid required security by fixed assets.

The second most common complaint about government programs was that the processing of applications was much too slow and that cutting through the bureaucratic red tape took an immense amount of management time. Most small businesses stated they could ill afford to spend much management time seeking these funds. A number of private consultants have emerged specializing in assisting companies to secure government grants and loans. The fact that these consultants exist illustrates the point that the process consumes too much of the small businessman's time and effort. These consultants seem to be the finders of the government assistance area and typically charge a five percent fee for their services. However, the government oriented consultants do provide a valuable service in helping the small businessman prepare his application for funds and assisting him by taking it to the proper authority and helping him negotiate a grant or loan through all stages of the process.

Another major criticism from small businesses was that many firms which were obtaining money from the government did not deserve it. They criticized subsidization of large businesses and in particular American subsidiaries, which had more resources to devote to obtaining these government funds. Exhibit 9 contains data on the degree of foreign ownership of firms receiving grants from several federal programs. The degree of foreign ownership of these firms is indeed high, but this is the case with the total population of Canadian firms.[6]

This claim by users was substantiated to some degree during our study, since we found that the firms which made the most of government opportunities for capital were larger firms and especially American subsidiaries. Four American subsidiaries were interviewed who had used government grants and loans many times to finance larger projects, which may not have been undertaken without such government funding.

The most common criticism from small firms was that the personnel involved in government programs were "unbelievably conservative" in their approach to granting government aid. The Industrial Development Bank and all of the provincial lending institutions were cited. The interviews with government officials substantiated this criticism. The government programs are oriented toward expansion of established companies rather than high-risk situations.

Suggestions by Users

Many users had suggestions which were aimed at having government agencies assist small businesses with information and advice to locate sources of capital and help prepare applications or proposals for presentation to these sources. Providing assistance to small businesses through programs like the Counselling

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6. Foreign Direct Investments in Canada, op.cit., Chapter 1.

Assistance for Small Business program, which uses retired businessmen and volunteers who have had experience in raising capital from various sources, was one suggestion. This would essentially be an extension of the current CASE program, described in Appendix 1.

Surprisingly, very few of the users of government programs interviewed suggested more government aid. They observed rather that the government should concentrate on improving the process whereby small businesses get started and grow. These suggestions included reforming current government programs so that they suited the needs of small business more than they do at present. Users recommended that the Industrial Development Bank fulfil original objectives. But similar comments were aimed at most of the other government programs as well.

The most common theme in these comments by users was that the government is capable of providing non-financial assistance in the form of advice to potential users and references to potential sources of funds. The provision of assistance in gathering data required by potential investors and training in the preparation of a proposal using the data were common requests. Users commented that there was no single agency of the government which they could approach with respect to their problems. The departments of industry, both at the federal and provincial level, usually paid more attention to the problems of large businesses than to the small firms. They suggested the establishment of an agency like the American Small Business Administration as one possibility for directing attention to a solution of this problem.

In addition, many comments focused on the government's role in providing incentives to the private sector to become more oriented towards small business. These included government guarantees of loans, revision of tax legislation to give more incentive to investors in small business and changes in the institutional regulations which would permit financial institutions to become more responsive to the financial needs of small business. The latter institutions included especially the chartered banks which small businessmen criticized as offering very little help to them.

Conclusions and Recommendations

Government grant and loan programs, in general, do not provide much assistance to small businesses in the start-up and early development stage of their life cycle. All of the government programs examined require considerable collateral or security and usually require a track record of the company before granting such funds.

In addition, all government programs provided only debt financing to small businesses, even where they were authorized to issue equity financing. Most of the small businessmen surveyed did not suggest that the government programs other than the IDB should become involved in providing equity capital to small businesses.

The comments of the users were generally directed at improving the efficiency and the applicability to small business of existing government programs, so that small businesses were more eligible for funds provided by these programs and to assisting small businesses to improve the process by which financing could be obtained from private sources. This leads to further reinforcement for our recommendation that the government should establish a separate agency for small businesses which would serve primarily as a "clearing house". This agency would provide information to small businesses on how to prepare proposals to obtain funds and where to look for the most likely sources of capital. This referral service would apply to governmental programs, both federal and provincial, as well as to private sources of capital.

In addition, this agency would provide counselling, advice and training to improve the management ability of people in small businesses in Canada. The current analysts in many of the government programs seem to be quite capable of providing such assistance, but seldom do so within current programs because their function is to evaluate rather than to help prepare the proposals.

In conclusion, small businessmen in Canada thought that the federal and provincial governments should be concentrating their efforts more towards improving the process whereby private sources of capital can finance the development of small businesses in Canada, rather than creating new programs to add to the existing proliferation of such programs in Canada. When advised of the American Small Business Administration and their Small Business Investment Company program, most of the managers of small firms readily agreed that something similar was needed in Canada, but they were in agreement that the capital should come mainly from private sources rather than from government.

EXHIBIT 1

INCENTIVE PROGRAMS AND SIZE OF FIRMS

Feb. 28, 1972.

Size of firm by Sales Volume ($000)	PAIT	GAAP	IDAP	PEP
under 250	10	8.2	24	5
250-500	9	11.0	17	2
500-1000	8	20.5	7	17
1000-5000	24	37.0	26	49
5000 up	49	23.3	26	27
	100%	100.0%	100%	100%
	(1)	(2)	(3)	(4)

1. Based on 151 approved projects.
2. Based on 73 approvals.
3. Based on 42 approved applications.
4. Based on 41 approved applications.

Source:
Department of Industry, Trade and Commerce.

EXHIBIT 2

ANALYSIS OF PROGRAM PAYMENTS BY COMPANY SIZE AND BY INDUSTRY SECTOR

	IDAP				PEP			
Size of firm by Sales Volume (000)	Projects Approved No.	%	Commitment ($000)	%	Projects Approved No.	%	Commitment ($000)	%
under-250	12	22	173.7	14.5	3	3	40.7	3.0
250-500	8	15	107.2	8.9	2	2	4.5	0.3
500-1000	6	11	80.8	6.7	16	18	104.1	7.7
1000-5000	14	26	441.5	36.7	37	43	493.3	36.5
5000-$	14	26	398.4	33.2	30	34	709.9	52.5
	54		1201.6		88		1352.5	

BRANCH SECTOR								
Aerospace, marine & rail	6	11	119.9	10.0	4	5	72.0	5.3
Agric.fish & food	-	-	-	-	10	11	166.6	12.3
Apparel & textiles	-	-	-	-	41	46	320.7	23.7
Chemicals	2	4	27.5	2.3	3	3	41.8	3.1
Elec.&electronic	9	16	247.6	20.6	5	6	166.3	12.3
Machinery	12	22	202.7	16.8	6	7	132.6	9.8
Mech.transport	8	15	206.7	17.2	5	6	84.3	6.2
Wood products	14	26	321.4	26.8	4	5	112.8	8.4
Materials	3	6	75.8	6.3	10	11	255.4	18.9
	54		1201.6		88		1352.5	

EXHIBIT 2 (continued)

Size of firm by Sales Volume (000)	PAIT Projects Approved No.	%	Commitment ($000)	%	DIP Projects Approved No.	%	Commitment ($000)	%
under 250					28	5	5517	2.0
250-500	83	25	27793.7	26	18	3	933	0.3
500-1000	23	7	1978.5	2	75	13	7861	2.0
1000-5000	73	22	28824.6	27	136	24	18940	6.0
5000-$	149	46	47950.0	45	302	55	285117	90.0
	328		106546.8		559		318368	
BRANCH SECTOR								
Aerospace,marine & rail	18	6	18209.0	17	257	46	186219	59.0
Agric.,fish & food	18	6	1254.1	1	-	-	-	-
Apparel & textile	9	3	847.9	1	1	0.2	1	
Chemicals	41	12	7667.9	7	5	1	346	0.1
Elec.& electronics	80	24	46763.6	44	194	35	107031	34.0
Machinery	60	18	8708.0	8	62	11	17944	6.0
Mech.Transport	46	14	8719.5	8	38	7	6545	0.2
Wood products	16	5	4330.1	4	-	-	-	-
Materials	40	12	10046.7	10	2	0.3	282	0.1
	328		106546.8		559		318368	

Source:
Department of Industry, Trade and Commerce.

Exhibit 3

INDUSTRIAL DEVELOPMENT BANK STATISTICS 1968-72

IDB LOANS BY SIZE	Fiscal 1968	Fiscal 1969	Fiscal 1970	Fiscal 1971	Fiscal 1972
$25,000 or less	46%	46%	51%	48%	48%
$25,000 to $100,000	46	45	42	45	45
Over $100,000	8	9	7	7	7
	100%	100%	100%	100%	100%
Average size of loan ($000)	48	51	46	44	45

PURPOSES OF CUSTOMERS' PROGRAMS	Fiscal 1968	Fiscal 1969	Fiscal 1970	Fiscal 1971	Fiscal 1972
Land and buildings	56%	53%	53%	47%	48%
Machinery and equipment	23	25	23	22	22
Increase in working capital	9	9	11	13	11
Refinancing of mortgages, liens, etc	7	6	6	9	8
Changes of ownership	4	6	6	8	10
All other programs	1	1	1	1	1
	100%	100%	100%	100%	100%

(In fiscal 1972 these programs required total financing of $376.2 million of which the IDB supplied $262.3 or 70%)

The number and amounts of loans by the IDB to all types of business in fiscal 1972 increased generally over the previous year:

IDB LOANS BY TYPE OF BUSINESS	Fiscal 1968	Fiscal 1969	Fiscal 1970	Fiscal 1971 No.	Fiscal 1971 Amount ($000)	Fiscal 1971 %	Fiscal 1972 No.	Fiscal 1972 Amount ($000)	Fiscal 1972 %
Manufacturing	29%	27%	23%	991	$55,625	22	1294	$72,758	22
Transportation and storage	4	3	4	166	7,874	4	177	10,177	3
Construction	6	6	5	239	9,728	6	298	9,606	5
Agriculture	8	6	7	338	11,415	8	416	16,479	7
Wholesale and retail trade	23	24	24	1081	37,109	24	1585	56,749	27
Tourist industry	14	18	18	901	44,601	20	1209	59,340	20
Other	16	16	19	733	29,628	16	910	37,201	16
	100%	100%	100%	4449	195,980	100%	5889	262,310	100%

CLASSIFICATION BY PROVINCE	NUMBER 1968	NUMBER 1969	NUMBER 1970	NUMBER 1971	NUMBER 1972	AMOUNT 1968	AMOUNT 1969	AMOUNT 1970	AMOUNT 1971	AMOUNT 1972
Newfoundland	31	38	81	87	149	1,315	1,290	2,100	2,563	4,892
Prince Edward Island	17	16	34	33	46	355	447	804	1,378	1,236
Nova Scotia	44	92	116	136	186	1,565	3,692	3,750	3,996	5,686
New Brunswick	63	120	85	112	142	2,124	5,119	3,521	3,488	5,039
Quebec	461	541	601	654	1,085	24,484	34,607	31,910	34,871	59,049
Ontario	833	863	978	1,216	1,568	41,579	45,003	46,490	49,723	65,124
Manitoba	127	111	101	156	151	5,912	5,072	5,440	7,941	8,091
Saskatchewan	129	123	112	138	140	5,054	4,855	3,513	4,591	5,179
Alberta	289	300	330	430	436	13,463	15,161	15,472	20,366	18,281
British Columbia	493	751	1,094	1,428	1,928	22,022	36,248	48,579	63,189	85,683
Yukon	17	22	23	43	42	688	1,253	1,087	2,614	2,905
N.W. Territories	11	11	29	16	16	1,692	693	1,962	1,260	1,145
	2,515	2,988	3,584	4,449	5,889	120,253	153,440	164,628	195,980	262,319

Exhibit 4

CLASSIFICATION OF IDB LOANS

	NUMBER						AMOUNT ($000)					
	1967	1968	1969	1970	1971	1972	1967	1968	1969	1970	1971	1972
Manufacturing:												
Foods and beverages	125	137	138	120	153	175	7,411	7,423	8,682	7,938	8,773	10,880
Tobacco and tobacco products	—	1	—	1	—	—	—	40	—	32	—	—
Rubber products	5	6	17	10	10	16	252	206	1,141	855	642	1,616
Leather products	13	8	13	13	9	21	577	364	809	434	369	908
Textile products (except clothing)	24	19	21	18	18	32	1,777	2,375	1,697	1,743	2,145	4,526
Clothing (textiles and fur)	35	27	35	28	40	50	2,727	1,444	2,439	1,510	1,768	2,521
Wood products	102	100	126	144	168	274	7,078	4,825	8,068	9,454	13,546	19,125
Paper products (including pulp)	22	7	18	18	13	28	1,516	272	2,609	1,279	938	1,636
Printing and allied industries	48	56	55	62	104	107	2,636	2,036	3,083	2,276	4,395	3,040
Iron and steel products (including machinery and equipment)	171	199	195	211	233	283	9,297	11,121	12,764	14,058	11,168	14,083
Transportation equipment	22	31	30	34	39	49	1,215	1,788	1,704	2,073	2,342	2,499
Non-ferrous metal products	7	11	7	8	12	7	841	484	439	635	547	187
Electrical apparatus and supplies	17	18	17	21	29	31	1,687	1,358	1,143	928	1,653	1,329
Non-metallic mineral products	34	41	39	52	52	60	1,361	3,049	2,474	2,477	2,706	3,983
Products of petroleum and coal	2	—	—	5	2	1	152	—	—	317	50	200
Chemical products	19	24	22	21	24	35	745	1,429	1,845	1,282	1,009	1,802
Miscellaneous manufacturing industries	47	50	65	71	85	125	1,939	1,992	3,114	3,663	3,574	4,419
Commercial air services	25	21	23	20	42	40	6,040	833	1,351	974	2,560	3,532
Warehousing (including refrigeration)	10	5	9	10	6	14	916	275	602	896	482	1,808
Other transportation and storage	63	77	77	96	118	123	6,255	4,456	6,775	4,596	4,832	4,837
Electric power, gas, water utilities	7	6	4	12	10	10	154	195	165	592	373	209
Mines (incl. milling), quarries, oil wells	18	17	21	25	30	29	1,129	1,123	1,529	1,182	1,424	2,226
Construction	127	157	174	194	239	298	4,945	6,163	7,181	7,799	9,728	9,606
Industrial buildings	79	145	201	222	286	357	4,443	10,026	10,749	12,318	14,672	18,144
Personal services	23	14	25	28	39	60	706	616	773	576	855	1,704
Forestry	16	11	6	15	24	30	661	257	193	566	1,060	1,170
Wholesale trade	159	154	204	220	262	338	8,129	6,992	10,322	10,978	13,396	16,993
Retail trade	342	430	501	639	819	1,247	13,455	14,781	17,225	21,520	23,713	39,756
Education and health services	20	48	34	66	67	63	1,189	1,912	2,143	3,664	3,102	2,738
Recreation services	31	42	39	57	84	99	1,504	1,876	2,115	2,620	4,157	5,699
Services to business management	31	28	40	57	71	78	716	801	1,594	1,731	2,003	2,154
Miscellaneous services	46	53	57	79	85	112	2,116	1,969	1,591	2,352	2,890	3,309
Agriculture	169	199	194	246	338	416	6,121	8,355	7,865	9,534	11,415	16,479
Fishing and trapping	7	11	13	21	17	31	143	208	195	389	485	810
Communications	17	7	16	13	13	12	1,075	365	778	616	456	787
Laundries, cleaners and pressers	32	47	56	74	91	99	1,059	2,086	1,572	2,429	2,308	2,894
Restaurants and other eating places	91	110	173	254	356	599	3,304	4,126	7,135	9,242	11,475	21,720
Hotels, motels and other lodgings	147	184	299	374	431	511	7,019	12,261	18,594	17,826	27,850	31,920
Theatres, bowling alleys, billiard halls	15	14	24	25	30	29	842	371	982	1,304	1,119	1,056
(Enterprises engaged in more than one type of business are classified according to major activity.)	2,168	2,515	2,988	3,584	4,449	5,889	113,132	120,253	153,440	164,628	195,980	262,310

IDB SUMMARY OF OPERATIONS 1944-1972
(Thousands of dollars)

Fiscal years ended September 30	November 1944 to 1964	1965	1966	1967	1968	1969	1970	1971	1972	Cumulative Total
LOANS AND INVESTMENTS										
Authorized during period	632,698	96,246	122,664	113,442	120,297	153,440	164,628	195,980	262,412	1,861,807
Less: cancellations and reductions	89,008	12,418	14,771	14,223	12,171	16,353	16,089	36,409	33,621	245,063
Net authorizations	543,690	83,828	107,893	99,219	108,126	137,087	148,539	159,571	228,791	1,616,744
Disbursements	503,678	81,141	98,143	96,631	105,466	122,376	150,961	156,168	193,997	1,508,561
Less: repayments and write-offs of principal	279,450	50,224	55,181	61,197	69,721	74,596	81,696	100,397	125,892	898,354
Increase in amounts outstanding	224,228	30,917	42,962	35,434	35,745	47,780	69,265	55,771	68,105	610,207
INCOME AND EXPENSE										
Income from loans and investments (interest and dividends)	77,508	16,638	19,293	22,863	26,396	30,575	38,257	47,505	55,103	334,138
Other income	4,827	469	482	583	659	535	619	1,237	1,514	10,925
Total income	82,335	17,107	19,775	23,446	27,055	31,110	38,876	48,742	56,617	345,063
Operating expenses										
Salaries and other staff expenses	21,186	3,884	4,794	5,300	5,916	6,762	7,618	8,881	10,826	75,167
Other	7,343	1,411	1,596	1,746	1,910	2,104	2,559	2,994	3,877	25,540
Total operating expenses	28,529	5,295	6,390	7,046	7,826	8,866	10,177	11,875	14,703	100,707
Cost of debentures	30,129	9,549	11,457	13,875	16,478	20,107	26,102	30,730	33,933	192,360
Net income before allowance for doubtful accounts	23,677	2,263	1,928	2,525	2,751	2,137	2,597	6,137	7,981	51,996
Allowance for doubtful accounts	6,194	1,323	1,393	1,891	1,976	1,764	2,097	4,158	4,369	25,165
Transferred to reserve fund	17,483	940	535	634	775	373	500	1,979	3,612	26,831
WRITE-OFFS										
Bad debts written off, net	1,695	573	393	641	726	1,264	847	758	1,269	8,166
YEAR-END BALANCE SHEET										
Loans and investments, including agreements for sale		255,328	298,415	334,744	371,350	419,232	487,486	543,147	611,505	
Less: allowance for doubtful accounts		−5,250	−6,250	−7,500	−8,750	−9,250	−10,500	−13,900	−17,000	
All other assets		6,703	6,698	6,061	7,597	3,773	10,467	14,522	14,717	
Total assets		256,781	298,863	333,305	370,197	413,755	487,453	543,769	609,222	
Capital, issued and paid up		38,000	41,000	44,000	47,000	51,000	53,000	55,000	58,000	
Reserve fund		18,423	18,958	19,592	20,367	20,740	21,240	23,219	26,831	
Debentures outstanding		195,400	232,800	262,500	293,600	331,500	394,100	445,500	501,700	
All other liabilities		4,958	6,105	7,213	9,230	10,515	19,113	20,050	22,691	
Total liabilities		256,781	298,863	333,305	370,197	413,755	487,453	543,769	609,222	

Exhibit 6

Department of Regional Economic Expansion

INCENTIVE GRANT APPLICATIONS

DISPOSITION OF APPLICATIONS AND
STATUS OF OFFERS - DECEMBER 1972

	MONTH	CURRENT FISCAL YEAR	INCEPTION TO DATE	%
STATUS OF APPLICATIONS				
Applications Received	105	1,953	6,936	100
Applications Withdrawn	81	848	2,066	30
Applications Rejected	54	643	1,575	23
Offers Made	54	787	2,665	38
STATUS OF OFFERS MADE				
Offers Made	54	787	2,665	100
Offers Lapsed	6	50	137	5
Offers Declined	2	55	199	7
Offers Accepted	39	749	2,198	79
STATUS OF OFFERS ACCEPTED				
Offers Accepted	39	749	2,198	100
Accepted Offers Declined or Withdrawn	7	125	241	11
Net Offers Accepted	32	624	1,957	89
STATUS OF NET OFFERS ACCEPTED				
Net Offers Accepted	32	624	1,957	100
No Payment Made			1,069	55
Partial Payment Made	36	310	847	43
Final Payment Made	6	41	41	2

Incentive Grants Offered as of December 1972 - $324.4 million
Incentive Grants Paid to Date - $72.7 million
Eligible Capital Costs - $1,616 million
Expected Direct New Jobs - 81,752

Exhibit 7

Department of Regional Economic Expansion

LOAN GUARANTEE APPLICATIONS

DISPOSITION OF APPLICATIONS AND
STATUS OF OFFERS - DECEMBER 1972

	MONTH	CURRENT FISCAL YEAR	INCEPTION TO DATE
STATUS OF APPLICATIONS			
Applications Received	3	63	199
Applications Withdrawn	3	42	73
Applications Rejected	1	21	55
Offers Made	1	12	23
STATUS OF OFFERS MADE			
Offers Made	1	12	23
Offers Lapsed	1	1	2
Offers Declined	-	2	2
Offers Accepted	-	8	16
STATUS OF OFFERS ACCEPTED			
Offers Accepted	-	8	16
Accepted Offers Declined or Withdrawn	-	1	2
Net Accepted Offers	-	7	14
STATUS OF NET OFFERS ACCEPTED			
Net Offers Accepted	-	7	14
Guarantees in Operation	-	2	3

Exhibit 8

Department of Regional Economic Expansion

AREA DEVELOPMENT INCENTIVES ACT

Applications for Incentives & Tax Holiday, by Region, at March 31, 1970

Region		Active Cases	New Investment in Fixed Assets	Average Investment in Fixed Assets $ millions	Direct Job Opportunities
Atlantic Provinces	Grant	342	$ 748,657,000	2.2	18,920
	Tax	33	88,465,000	2.7	2,745
Quebec	Grant	342	481,059,000	1.4	16,612
	Tax	39	154,139,000	0.4	2,979
Ontario	Grant	139	237,470,000	1.7	9,840
	Tax	93	223,943,000	2.4	8,453
Prairie Provinces	Grant	173	339,378,000	2.0	5,806
	Tax	5	2,998,000	0.6	472
British Columbia	Grant	127	154,658,000	1.2	4,935
	Tax	4	2,040,000	0.5	186
	Grant	1,123	1,961,222,000	1.7	56,113
	Tax	174	471,585,000	2.7	14,835

EXHIBIT 9

SAMPLE OF FEDERAL GRANTS
BY COUNTRY OF CONTROL OF FIRM RECEIVING GRANT

IRDIA GRANTS
($000)

	1967-68	1968-69	1969-70	1970-71
Non-resident owned or controlled firms	976.6	8,554.7	9,690.4	19,221.7
Canadian owned or controlled firms	975.4	10,773.6	12,400.1	24,149.1
Ownership unknown	179.3	264.0	909.5	1,352.8
Total	2,131.3	19,592.3	23,000.0	44,723.6

PAIT INCENTIVES

	1965-66	1966-67	1967-68	1968-69	1969-70	Total
	$000	$000	$000	$000	$000	$000
Canadian owned or controlled firms	147.0	1,596.3	2,815.6	3,401.0	3,264.0	11,223.9
Non-resident owned or controlled firms	281.2	2,999.7	3,549.3	903.0	2,005.0	9,738.2
Totals	428.2	4,596.0	6,355.9	4,304.0	5,269.0	20,962.1

DEFENCE PROGRAMME GRANTS

	Number of Firms Benefitting		Amount $000	
Programme	Canadian	Non-Resident	Canadian	Non-Resident
IMDEP	50	38	5,659.7	15,356.9
DDSP	23	29	7,382.5	62,045.9
DIP	62	47	3,528.2	26,060.8
Total	97*	64*	16,570.4	103,463.6

* Net number of firms benefitting; i.e., some firms benefitted under more than one programme.

Source: Foreign Direct Investment in Canada, Government of Canada

APPENDIX I

FEDERAL GOVERNMENT ASSISTANCE PROGRAMS

1. Building Equipment, Accessories and Material Program (B.E.A.M.)

Purpose of the Program

To increase productivity and efficiency in the manufacturing and use of building equipment, accessories and materials.

Form of Aid Provided

Free information to the construction and building industry with a means for storing, retrieving and disseminating information vital to the effective conduct of its business.

Areas where information is provided:

- construction information systems
- modular coordination and standardization
- industrialized building techniques and systems
- development and expansion of export markets for Canadian buildings, building components and expertise
- encouragement of building design excellence

2. Industrial Research Assistance Program (I.R.A.P.)

Purpose of the Program

To assist in developing long-term applied research in the sciences and engineering and in the development of proto-types and processes.

Form of Aid Provided

Grants

Criteria for Eligibility

Program is assessed on its scientific merits and the capabilities of the company and its staff.

Company must be incorporated in Canada and all research must be conducted in Canada.

Amount of money available if the company qualifies

Grant for salaries and wages of the technical staff. Assistance continues on an annual basis depending on satisfactory performance.

Tax Treatment

I.R.A.P. grants exempt from income tax.

3. Automotive Adjustment Assistance Program (A.A.A.)

Purpose of the Program

To assist Canadian automotive producers and automotive parts producers to expand their operations and make them more efficient.

Form of Aid Provided

Term loan.
This program terminates June 30, 1973.

Criteria for Eligibility

Cannot obtain necessary capital elsewhere on reasonable terms and conditions for expansion or re-equipping.

Must show an opportunity to supply the auto parts market.

Must be an original equipment parts manufacturer that has been affected by the Canada-United States agreement on automotive products.

Repayment Terms

Related to company's capacity to repay. May extend for a period up to 20 years. Lending rate is the rate to crown corporations plus 2%.

Tax Treatment

Remit duties and sales tax paid on duties on imported production machinery and equipment not available from Canadian producers.

4. Machinery Program (MACH.)

Purpose of the Program

To enable Canadian industrial machinery and equipment users to import capital equipment, tools and accessories which are not available from production in Canada, on a duty remitted basis.

To encourage Canadian production of such industrial machinery and equipment.

To increase efficiency of Canadian industry by enabling machinery users to acquire advanced equipment at the lowest possible cost.

To give Canadian machinery producers tariff protection.

Form of Aid Provided

Remission of duty paid above the first $500,000 of value for duty on machinery eligible for remission.

Criteria for Eligibility

Remission is in the public interest. The machinery is not available from production in Canada.

5. General Adjustment Assistance Program (G.A.A.P.)

Purpose of the Program

To assist companies injured by Kennedy Round tariff changes.

Form of Aid Provided

Guarantees, loans and grants for consulting help.

Criteria for Eligibility

Manufacturers with viable adjustment projects for which financing is required but unavailable from other sources on reasonable terms and who:

a) have significant export opportunities arising out of the Kennedy Round agreements,

b) have been or could be injured as a result of Kennedy Round tariff reduction,

c) are manufacturers of textile, clothing goods or footwear and wish to improve their competitive position in domestic or export markets or wish to adapt efficiently to disruptive import competition.

Tax Treatment

Reimbursed consultants' fees are not deductible.

6. Industrial Research and Development Incentives Act (I.R.D.I.A.)

Purpose of the Program

To provide additional incentives for scientific research and development.

Form of Aid Provided

Cash grant.

Criteria for Eligibility

Must be a taxable corporation incorporated in and carrying on business in Canada. Proprietorships, partnerships and unincorporated associations are not eligible, nor is the foreign corporation with a branch operation in Canada.

Expenses must have been incurred. Company must be free to exploit the results of the research and development in Canada and all export markets. Must be a chance of improving the product or process by incorporating a significant technical advance.

Capital expenditure on scientific research and development that qualify.

Amount of money available if the company qualifies

Grant equal to 25% of the aggregate of

a) capital expenditures on research and development

b) eligible current expenditure in excess of the average of such expenditures incurred during the base period.

Applications must be submitted within 6 months of the applicant's year-end and the company must provide proof of expenditures.

Tax Treatment

Grants are exempt from income tax and the amount of grant received by the corporation in respect of a fixed asset does not reduce its capital cost for income tax purposes.

7. Program for Advancement of Industrial Technology (P.A.I.T.)

Purpose of the Program

To assist in the development of products and processes which improve productivity and directly contribute to the economic growth.

Form of Aid Provided

Grants

Criteria for Eligibility

All companies incorporated in Canada that carry out development projects in Canada and are exploited in Canada. Costs incurred prior to submission are not eligible. The project must be technically and commercially feasible. The company must have the necessary management and technical skills to develop and exploit the results. The company must have adequate facilities. The company must be financially sound. Capital costs incurred for the acquisition of general purpose facilities and equipment, and expenses related to production and marketing activities are not eligible for support under the program.

Amount of money available if the company qualifies

50% of all associated development costs.

Tax Treatment

Only the company's share of cost is deductible under Section 72. However, should the company be required to pay P.A.I.T. grants, it will be entitled to deduct such repayments under Section 72.

8. Defense Industry Productivity Program (D.I.P.)

Purpose of the Program

To enhance the technological competence of the Canadian defense industry in its export activities by providing financial assistance to industrial firms for selected projects from research and development through production.

Form of Aid Provided

Grants

Criteria for Eligibility

The machinery acquired must make a significant contribution to increased productivity. Assistance may be provided for the following:

a) Development of defense products for export,

b) Acquisition of modern machine tools to increase efficiency,

c) Assistance with pre-production expenses to establish manufacturing sources for defense products in Canada for export markets.

Amount of money available if company qualifies

50% of the cost involved in acquiring the equipment. The department initially absorbs the total acquisition costs subject to repayment, without interest, by the company of its share over a five year period.

9. Pharmaceutical Industry Development Assistance (P.I.D.A.)

Purpose of the Program

To assist the Canadian Pharmaceutical Industry to adopt the latest technology and the most modern management techniques as well as to encourage advances in research and development.

Form of Aid Provided

Direct loans at commercial interest rates.

Criteria for Eligibility

A P.I.D.A. Loan may be received if:

a) You have a plan for re-organization or expansion involving merger, corporate or financial restructure, or improved capabilities in marketing, manufacturing, or research and development,

b) The plan will result in the manufacture and effective marketing of high quality, safe and effective prescription drugs at more competitive prices,

c) You can show that you need a loan to carry out the plan,

d) You cannot obtain sufficient capital to carry out the plan from other sources on reasonable terms,

e) You have, or can acquire, all needed capabilities, whether technical, financial, managerial or marketing,

f) The pharmaceutical operations will be carried out by a company or group of companies incorporated in Canada.

Repayment Terms

The direct loan is for terms of up to 20 years for purchase of buildings and real-property or 10 years under other circumstances. The interest rate will be equal to or greater than the interest rate on government loans to Crown Corporations but may not exceed that rate by more than 2 1/4%.

10. Industrial Design Assistance Program (I.D.A.P.)

Purpose of the Program

To improve the quality of Canadian product design, thereby advancing Canadian industry and expanding its sales. Create an environment in Canada which will attract and retain industrial design talent.

Form of Aid Provided

Grants

Criteria for Eligibility

The applicant company must have been incorporated in Canada. Research must be conducted in Canada. The applicant company must have a satisfactory organization and facilities, also satisfactory financial resources. The project must be classified as an Industrial Design function.

Amount of money available if the company qualifies

50% of the industrial design operational and administrative costs. Capital costs of any kind are excluded. The grant is not made until after the costs have been incurred.

Tax Treatment

The I.D.A.P. grants are exempt from income tax. The expenditures incurred on a project financed under I.D.A.P. may be deducted in computing the income of the recipient of the grant under Section 72 of the Income Tax Act if the expenditures exceed the amount of grant received by the company.

11. Program to Enhance Productivity (P.E.P.)

Purpose of the Program

To induce improved productivity in manufacturing and processing industries in Canada and to undertake intensive studies of significant and imaginative efficiency improvement projects.

Form of Aid Provided

Grants up to a maximum of $50,000 to support up to 50% of the approved costs of a feasibility study. Capital costs of any kind are excluded.

Eligibility Criteria

Must be a company incorporated in Canada. The project must involve a significant departure from the company's traditional productivity improvement practices and also involve only existing available technology. There exists a marked but unproved potential for significant increase in productivity but uncertainty as to its profitability. A feasibility study is required before a decision can be made.

Successful completion of the project could result in:

a) greater industrial strength and improved exports,

b) expansion of sales and production in high productivity operation,

c) satisfactory return on production and sales.

12. Ship Construction Subsidy Regulations (S.C.S.R.)

Purpose of the Program

To provide protection and incentive to the Canadian shipbuilding industry.

Form of Aid Provided

Grants

Criteria for Eligibility

The shipbuilder must be a Canadian citizen or company incorporated in Canada and must be building ships in Canada. Commercial shipbuilding in Canada.

13. Development of Management Courses

Purpose of the Program

To help non-profit professional, industry, business, or management associations develop management retraining or upgrading courses of high quality.

Form of Aid Provided

Assistance in the form of government grants, to a maximum of $50,000. Development costs eligible for such assistance include:

a) professional fees paid in the development or revision of the course,

b) costs of visual and audio aids to be used in the course, but not the costs of printing textbooks and notebooks.

Criteria for Eligibility

1. Applicant must be a non-profit professional, industry, business or management association that can contribute significantly to the improvement of managerial competence in Canadian industry.

2. Applicant must be able to implement the course successfully.

3. Development of the course must not contribute to an undesirable proliferation of similar courses.

14. Counselling Assistance to Small Enterprises (C.A.S.E.)

Purpose of the Program

At present, C.A.S.E. is operating on a pilot project basis in

Montreal and Winnipeg.

C.A.S.E. provides an opportunity for the owners and managers of small businesses engaged in manufacturing or tourism to benefit, at nominal cost, from a service provided by retired business executives selected for their management experience.

Form of Aid Provided

Through C.A.S.E., managements of small companies can discuss their particular problems with experienced businessmen, explore new ideas to help their businesses grow and examine new methods for improving productivity.

Each C.A.S.E. counsellor receives $30 a day for his counselling assistance, including any assistance he may render in implementing his recommendations. The small business pays two-thirds of the daily $30 fee. The government pays the remaining costs.

Critieria for Eligibility

To be eligible a firm must:

a) Be a manufacturer or be in the tourist industry,

b) Have fewer than 50 employees and no more than $5 million in sales in its most recent complete fiscal year.

15. Program for Export Market Development - Section "A" - (P.E.M.D.)

Purpose of the Program

To increase the level of Canadian participation in foreign capital projects by sharing with companies expenses incurred when competing during the precontractual phases of approved projects.

The term "capital projects" is intended to describe facilities, systems and other complexes whose construction entails the provision of skilled services, engineering products and other capital goods.

Form of Aid Provided

The government's contribution will normally be 50% of the expenses incurred in the precontractual phases of actual or potential projects and will normally fall into the categories of exploratory studies and preparation of initial proposals and bids.

In the event that a company that has received assistance is successful in obtaining the business sought, repayment of the government's contribution will be required in two equal payments, one due six months after the date of the contract and the other twelve months after obtaining the contract.

Repayment is not required in instances where a company is not successful in obtaining the contract sought.

Criteria for Eligibility

1. The applicant company must be currently established and operating in Canada.

2. The applicant company must have ability, or demonstrated potential for competitive performance in foreign markets for the products or services concerned.

3. The applicant company must have satisfactory financial and management strengths.

4. The project must apply to goods or services for which competent Canadian sources already exist.

5. The project must promise significant Canadian content.

6. The project must have a reasonable probability of success.

7. The project must appear financially sound.

8. Desirable for project to provide opportunity for follow-on business.

9. Military projects are not normally eligible.

10. The project must make "good business sense".

11. Collaborative applications are eligible.

12. Project must represent an increase in the normal level of applicant's exploratory activities.

16. Program for Export Market Development - Section "B" - (P.E.M.D.)

Purpose of the Program

The purpose of Section "B" of P.E.M.D. is to bring about a sustained increment in the export of Canadian products, especially manufactured goods.

Form of Aid Provided

The government will share, with Canadian companies, eligible expenses incurred in previously approved projects which aim to:

Part I. Identify and more precisely define a potential export market opportunity, appropriate to the abilities of the Canadian company.

Part II. Adapt the Canadian company's marketing methods to the requirements and practices of an export market.

In the event that a company that has received assistance is successful in obtaining export business, repayment of the Department's contribution will be required at a rate of 1% of sales of the product identified during a period of up to three years, to the total of the contribution.

Repayment is not required in instances where a company is not successful in obtaining export business of the kind described in the application.

Criteria for Eligibility

1. The company must be currently established and operating in Canada.
2. Have ability or demonstrated potential for competitive performance in foreign markets.
3. Have satisfactory financial and management strengths.
4. Apply to goods or services for which competent Canadian sources and/or capabilities already exist.
5. Promise significant Canadian content.

* 6. Have a reasonable probability of success.

* 7. Appear financially sound.

* 8. Form part of an overall company plan.

9. Make "good business sense".
10. Represent an extension of the normal efforts of the applicant in the export field.
11. Promise a net increment in exports.

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* These criteria apply only to applications under "Part II Marketing Adjustment".

17. Program for Export Market Development - Section "C" - (P.E.M.D.)

Purpose of the Program

The objective of the "Incentive for Participation in Trade Fairs Abroad" is to bring about a sustained increment in the export of Canadian goods and services by increasing the level of participation by Canadian companies in trade fairs outside Canada.

Form of Aid Provided

The department will share, with Canadian companies eligible expenses incurred in previously approved projects which aim to effect an increment in the export of goods and services.

Criteria for Eligibility

The criteria for eligibility are very similar to the requirements indicated in Sections "A" and "B" of the program.

18. Fashion Design Assistance Program (F.D.A.P.)

Purpose of the Program

To increase the international competitiveness of Canadian apparel, textile, leather and footwear industries by:

1. encouraging greater Canadian design creativity and upgrading product quality,

2. building a prestige image of creative Canadian fashion design to attract domestic and foreign buyers,

3. providing an environment to encourage and retain Canadian fashion design talent.

Form of Aid Provided

To give trained Canadian fashion designers the work climate that will foster creative design in Canada. It will be carried out by studies of training facilities and job opportunities to identify needed improvements and through bursaries for advanced studies in fashion design.

Promotion of good Canadian design and workmanship. All designs accepted as examples of good Canadian fashion are identified by a logo tag.

19. Shipbuilding Temporary Assistance Program (S.T.A.P.)

Purpose of the Program

A program of grants to shipbuilders constructing vessels for foreign registry.

Form of Aid Provided

The maximum grant is 16% of audited cost for vessels of up to 25,000 gross tons and 13% for vessels of more than 25,000 gross tons.

Criteria for Eligibility

There are restrictions concerning Canadian content and minimum size, details of which can be obtained from the Regulations. These grants are available on vessels completed before October 31, 1975 and contracted for prior to March 31, 1973.

20. Department of Regional Economic Expansion (D.R.E.E.)

Purpose of the Program

To reduce the economic and social disparities between various regions of Canada. The Minister of Regional Economic Expansion is responsible for "economic and social adjustment in areas requiring special measures to improve opportunities for productive employment and access to those opportunities".

Form of Aid Provided

In 1969, several programs were terminated, notably the Atlantic Development Board, the Area Development Agency and the Fund for Rural Economic Development, but provided that the new Department would be responsible for carrying their current activities through to completion.

The D.R.E.E. programs areas can be classified under four main headings:

1. Planning and Programming: To develop the means of improving opportunities, and making them effective in slow growth areas.

2. Industrial Incentives: To make investment in viable industries more attractive in the slow-growth regions and thus improve employment opportunities.

3. Infrastructure Assistance: To provide the incremental social capital that is necessary to better opportunities.

4. Social Adjustment and Rural Development: To assist people in taking advantage of new opportunities and in increasing their incomes from the more effective utilization of rural resources.

The specific programs offered by the Department are as follows:

1. Incentives to Industry: To encourage new productive employment. The incentives are designed to offset the initial

disadvantages of an industrial investment in the areas where additional employment is most needed. Most manufacturing and processing industries are eligible for both incentive grants and loan guarantees. Loan guarantees, but not incentive grants can be provided for hotels, convention centres and recreational facilities. Maximum incentive grants vary according to region.

A. Atlantic Region: Up to 30% of capital cost, for expansions or modernizations: up to 35% of capital cost, plus up to $7,000 per job created, for new plants or new product expansions.

B. Standard Region: Up to 20% of capital cost, for expansions or modernizations; up to 25% of capital cost, plus up to $5,000 per job created, for new plants or new plant expansions.

C. Southwestern Quebec, including the cities of Montreal and Hull, and the Eastern Ontario counties of Stormont, Glengarry and Prescott: Up to 10% of capital cost for expansions or modernizations; up to 10% of capital cost, plus up to $2,000 per job created, for new plants or new product expansions.

2. Special Area Programs: There are 22 special areas where faster growth can have major repercussions through eastern Canada generally, the plans provide for roads, bridges, water and sewer systems, serviced industrial and residential land, schools, tourist facilities, industrial parks, and other facilities to strengthen the economic and social effects of the region.

3. Prairie Farm Rehabilitation Act: Provides technical and financial assistance for farm water projects and small community water storages.

4. Agriculture and Rural Development Act: Programs undertaken are such things as alternate land use, soil and water conservation and general rural development associated with creating income and employment opportunities.

5. The Canada Land Inventory: The object of the CLI is to produce data on land capability, primarily for land use and rural development planning.

6. The Canada Newstart Program: This program was introduced to experiment with and isolate effective and efficient techniques and methods of social and human development. To achieve this aim, six autonomous, provincially incorporated pilot projects were established. Considerable experimentation with methods of adult basic training in academic and vocational education and life skills; recruitment; motivation; counselling; and job placement have been performed.

Criteria for Eligibility

The company must locate in specified regions. The operations of the company must create new jobs. The company must be in manufacturing, processing or commercial industries.

Amount of money available if company qualifies

Maximum primary development incentives: 20% of those approved capital costs, or $6,000,000 whichever is the lesser amount.

Maximum secondary development incentives: 5% of those approved capital costs plus $5,000 for each new job created.

Maximum combined development incentives: $30,000 for each new job created, $12,000,000 or 1/2 of the capital to be employed in the operation, whichever is the lesser amount.

21. Scientific Research

Purpose of the Program

To encourage scientific research in Canada.

Form of Aid Provided

Deduction for purposes of income tax under Section 72:

1. All current expenditures on research made in Canada during the year.

2. Capital expenditures made in Canada in that year on scientific research relating to the business.

Criteria for Eligibility

The activity must fall within the normally recognized field of science not specifically included. The work must be carried out by persons with the requisite training and experience who are skilled in the application of the scientific method. The work must be carried out in a systematic fashion. The uncertainty of the results must be removed through systematic investigation and analysis.

22. Industrial Development Bank

Purpose of the Program

To provide a source of medium and long-term finance for business unable to raise funds from other sources on reasonable terms and conditions. Financing of small business to assist in fixed asset expenditures and working capital assistance. To supplement the services of other lenders and sources of financing.

Form of Aid Provided

Loans may be provided to finance the purchase of fixed assets, to strengthen working capital, to finance the establishment of new businesses or to finance a change of ownership.

I.D.B. can provide financing by purchasing some of the common or preferred shares or convertible debentures of a business, usually provided along with a term loan secured by the fixed assets of the business.

I.D.B. can enter into or participate in underwriting agreements when a public issue would be the appropriate method of financing but could not be marketed on reasonable terms and conditions without the assistance of I.D.B.

In addition, I.D.B. through its Advisory Services program, helps promote good management practices in small and medium sized Canadian businesses.

Criteria for Eligibility

Sound proposal and capable management. Owners must have reasonable amount invested. Borrower must be unable to obtain sufficient funds on reasonable terms and conditions. Borrower must be able to provide security for the loan. Will not lend for purposes of residential development.

Amount of money available if the company qualifies

Average amount is $100,000 but a ceiling does not exist.

Repayment Terms

Generally over 5-12 years at conventional lending rates, however rates increase as the amount of the loan increases.

23. Export Development Corporation (E.D.C.)

Purpose of the Program

1. To insure Canadian firms against non-payment when Canadian goods and services are sold abroad.

2. To make loans to foreign purchasers of Canadian capital equipment and technical services.

3. To guarantee financial institutions against loss when they are involved in an export transaction by financing either the Canadian supplier or the foreign buyer.

4. To insure Canadians against loss of their investments abroad by reason of political actions.

Form of Aid Provided

Export trade falls into these categories; bulk commodities trade, consumer goods trade, advisory or technical services, capital goods trade, and capital construction projects. The E.D.C. has been established to provide the Canadian exporter with credit insurance, guarantee and loan facilities.

The E.D.C. is comprised of three main divisions:

1. Export Credits Insurance Division: E.D.C. may insure Canadian exporters against non-payment when they grant credit to foreign buyers. In the case of goods or services sold on short term credit, a comprehensive policy is issued which covers an exporter's entire export sales for one year. The E.D.C. normally covers a maximum of 90% of the amount of the loss.

2. Export Finance Division: E.D.C. makes long term loans to foreign purchasers, or guarantees private loans to foreign purchasers at internationally competitive interest rates. E.D.C. may make loans to foreign national development banks for relending to importers in their respective countries to enable them to buy Canadian capital goods.

   The transaction must be worth $1 million or more. The transaction must have a Canadian material/labour content of not less than 80%.

3. Foreign Investment Insurance: E.D.C. offers insurance against certain political risks of loss of Canadian investments abroad. Three categories of risk are covered. Inconvertibility, or ability to repatriate earnings or capital, expropriation and insurrection, revolution or war. The normal co-insurance to be carried by the investor is 15%.

24. Small Business Loans

Purpose of the Program

To help small business to obtain term credit for a wide range of business improvement purposes.

Form of Aid Provided

Secured term loans.

Criteria for Eligibility

Proprietorship, partnership or a limited company may borrow. Annual gross revenue must not exceed $500,000 during the year in which the application is made.

Types of Loans

Fixed equipment loans
Movable equipment loans
Premises loans

Terms of Repayment

Maximum period is 10 years at conventional lending rates.

25. Farm Improvement Loans

Purpose of the Program

To provide farmers with credit for the purchase of agricultural implements and a wide range of farm improvement projects. To enable farmers to raise the efficiency of their farming operations.

Form of Aid Provided

Term loans.

Criteria for Eligibility

Only a farmer can borrow. Loans must be for:

1. Purchase of agricultural implements
2. Purchase of livestock
3. Purchase or installation of agricultural equipment or a farm electric system
4. Construction, repair or alteration of farm buildings
5. Purchase of additional loand
6. Other projects for farm improvement and development

The applicant must provide a reasonable portion of the cost of the purchase or project from his own resources.

26. Fisheries Improvement Loan

Purpose of the Program

To supply financing to fisherman for a variety of fisheries improvement projects.

Form of Aid Provided

Term loans.

Criteria for Eligibility

Only a fisherman may borrow. Loans may be made for:

1. Purchase of a fishing vessel
2. Purchase or construction of fishing equipment
3. Motor repair and overhaul of fishing vessel
4. Purchase or construction of a shore installation
5. Development or improvement of a primary fishing enterprise

The applicant must provide a reasonable portion of the cost of the purchase or project from his own resources.

27. Incentive Programs North of 60

Purpose of the Program

The government has developed a series of incentive programs designed to aid both companies and individuals in exploration and development activities North of 60. These programs are administered by the Northern Economic Development Branch of the Department of Indian Affairs and Northern Development. There are six programs administered by the Department:

1. Northern Roads Network Program: The program involves the development of communication roads to provide a primary road network in the area, and lateral roads which lead from this primary network to areas where resource exploration, development or exploitation are taking place.

2. Northern Mineral Exploration Assistance Program: This program is designed to encourage the investment of domestic risk capital in both mineral and oil and gas exploration North of 60. Aid is provided in the form of a grant which may not exceed 40% of the cost of an approved exploration program.

3. Prospector's Assistance Program: Prospectors may be provided with grants of up to $900 per year to assist in outfitting and transportation to their area of activity. A prospector must spend a minimum of 60 days in the field and is required to submit a diary and report to receive final payment.

4. Northern Resource Airports Program: Cost sharing agreements for the establishment of airports may be made between the federal government and a natural resource development company.

5. Other Programs and Incentives: The government will in some cases finance economic feasibility studies of proposed northern primary production operations.

6. Small Business Loan Funds: Under the plan, up to $300,000 will be lent annually in each territory from the funds to businesses already operating or to enterpreneurs starting a new business.

   Such businesses as hotels, laundries and restaurants, municipal services and small manufacturing plants will be able to take advantage of the funds. The interest rate will be such that the scheme is self-sustaining except for administrative costs connected with the provision of management advice, which will be absorbed by the government.

28. Canadian Film Development Corporation

Purpose of the Program

The Corporation recognizes two main categories for its assistance:

1. Feature films designed for release in major motion picture theatres and on television in Canada and abroad to be assisted by investments and loans;

2. Feature films on low budgets produced primarily for the purpose of developing new talents to be assisted by special investments.

Form of Aid Provided

1. The Corporation's contribution will rarely exceed $200,000 and should not be more than 50% of the cost of production of the completed film.

2. Guaranteed distribution in Canada is a condition of investment.

3. In principle, all investments will be recovered pari passu from the returns of the film.

4. Depending on availability of funds, priority will be given to films also contracted for television release or films with a television potential, particularly on the international market.

29. Defense Industrial Research Program

Purpose of the Program

To assist companies seeking support for research projects oriented primarily to defense technologies. The objective is to improve the capability for innovation in Canadian industry.

Criteria for Eligibility

The primary criteria for selection are:

1. The extent of defense interest
2. The scientific feasibility and quality of the proposed research project
3. The calibre and experience of the technical staff
4. The potential for exploitation of the research in both defense and commercial applications.

Form of Aid Provided

Normally one half of the overall direct costs of the program.

APPENDIX II

PROVINCIAL GOVERNMENT ASSISTANCE PROGRAMS

BRITISH COLUMBIA

1. Department of Industrial Development, Trade and Commerce

Purpose of the Program

To provide services for the encouragement of industry, development of trade and the collection and publication of statistics.

Form of Assistance Provided

Assists firms to establish new industries and survey foreign and domestic markets.

2. British Columbia Development Corporation

Purpose of the Program

To create, develop and increase income, employment, tax revenue, and other economic benefits to the province by encouraging and assisting in the establishment, expansion and continued operation of industrial enterprises in the province.

Form of Aid Provided

1. Loans, loan guarantees, mortgages, and shares.
2. Acquire, develop, rent or sell land, buildings, machinery, etc.
3. Other financial and technical assistance.

3. The Copper Bounty Act

Purpose of the Program

To serve as an incentive to encourage more intensive processing of mineral products within British Columbia.

Form of Aid Provided

One cent per pound bounty paid on blister copper or refined copper within the province.

4. The Iron Bounty Act

Purpose of the Program

Same as the Copper Bounty Act.

Form of Aid Provided

$2.00 per ton on iron from ore mined out of the province. $5.00 per ton on ore mined within the province.

ALBERTA

1. Alberta Opportunity Company

Purpose of the Program

The promotion of economic growth in the province by stimulating the establishment of new businesses and aiding in the expansion of existing enterprises.

Form of Aid Provided

1. Capital loans to a level of 80% (maximum $500,000) at commercial rates.
2. Working capital loans to $500,000.
3. Inventory financing to $500,000.
4. Research and development loans to a level of 50% (maximum $10,000)
5. Loan guarantees
6. Business management counselling services.

Criteria for Eligibility

1. Company must be located within Alberta.
2. Proposal must be economically viable.
3. The availability of security.

2. Industrial Development Incentives Program

Purpose of the Program

To equalize the opportunities to attract or develop industries throughout Alberta.

To stimulate the industrial development of non-metropolitan areas of Alberta.

To provide financial resources for the development or expansion of industry in slow growth areas.

To assist in the development of secondary industry engaged in manufacturing.

Form of Aid Provided

Interest free loan, which may be forgivable.

Criteria for Eligibility

Manufacturing must be conducted in Alberta.
The economic impact of the project on the area must be significant.
The management must be capable.
The company must not be able to finance the project by other means.

Repayment Terms

Term of loan is 5 years, during which period no interest is charged and no repayment of principal is required.

Repayment of incentive loans may be forgiven entirely following five years of successful operation by the recipient.

3. The Native Co-Operative Guarantee Act Chapter 256

Purpose of the Program

To assist the productive operations undertaken by a co-operative association of Indians or Metis.

Form of Aid Provided

Loans

Criteria for Eligibility

The loan is required for productive purposes. There is not any distribution of earnings or profits without consent.

Repayment Terms

The Lieutenant Governor in council may authorize the Provincial Treasurer to guarantee on behalf of the Province the repayment of the whole or part of money borrowed by the association and interest and take as security any real or personal property.

4. The Co-Operative Marketing Association Guarantee Act

Purpose of the Program

To guarantee on behalf of the Province of Alberta, the payment of any sums borrowed for acquiring land, factories, warehouses, machinery or equipment.

5. Alberta Commercial Corporation

Purpose of the Program

To provide financial assistance to Alberta industries which may be unable to obtain suitable financing through other sources. Also provides guidance to small manufacturers and producers in their management problems.

To assist the growth of the tourist industry.

Form of Aid Provided

For small manufacturers to provide financing for inventories, plant equipment, plant-sites, including land and buildings.

Term loans.

Management guidance is without cost.

Repayment Terms

8% per annum with conventional terms.

SASKATCHEWAN

1. The Industry Incentive Act

Purpose of the Act

To encourage the establishment, expansion and modernization of industry in certain areas of Saskatchewan.

Form of Aid Provided

A six year, interest free loan which is forgiven at 10 per cent per year for the first 5 years and then completely forgiven in the sixth year, providing certain conditions are met.

Criteria for Eligibility

Manufacturers who qualify as to nature of operations and who wish to establish, expand or modernize outside the Federal Incentives area.

Amount of Money Available

a) $5,000 for each job created
b) 20% of the capital cost, or
c) $300,000
whichever is least.

2. Saskatchewan Economic Development Corporation

Purpose of the Program

To provide a source of financial assistance for industrial enterprises wishing to expand or establish their operations in Saskatchewan.

Form of Aid Provided

Mortgage loan.

Criteria for Eligibility

Primary or secondary manufacturers.
Certain specialized agricultural businesses.
The financing must be required for a business in Saskatchewan.
The funds must not be available elsewhere on reasonable terms and conditions.
The applicant business must be profitable and financially sound.
The owner's of the business must have a reasonable investment and there must be sufficient assets to provide reasonable security.
If benefits would accrue to the province by increasing employment, replacing inputs or stimulating exports.

Repayment Terms

Term up to ten years depending on ability to repay. Repayment by monthly installments of principal plus interest.

3. Industry and Commerce Development Act

Purpose of the Program

To make loans and grants to assist in, or provide for, the continuation of a business enterprise if threatened and its loss would disrupt the social and economic base of the community.

Form of Aid Provided

Loans and grants for:

1. modernization, refurbishing or expansion of small businesses,
2. to assist in the establishment of new businesses in areas of the province of slow economic growth,
3. promotion or development of the tourist industry,
4. consulting service by contract for
   (i) management training programs
   (ii) marketing, accounting, etc.

Criteria for Eligibility

1. Establishment in a city having less than 35,000 inhabitants.
2. Does not qualify under the Federal Regional Development Incentives Act.

4. Aid to Trade Program

Purpose of the Program

To stimulate the sale of Saskatchewan-made products and services. Its basic purpose is to increase the flow of money into the province and help create new employment.

Form of Aid Provided

Financial assistance to firms who wish to do the following:

1. exhibit their products and services in new products,
2. explore foreign markets and investigate sales opportunities,
3. ship sample merchandise to potential markets,
4. bring foreign buyers to Saskatchewan,
5. undertake a market feasibility study.

MANITOBA

1. Manitoba Development Corporation

Purpose of the Program

To promote the establishment and expansion of new and existing processing and manufacturing industries, to the tourist accomodation industry and to community development corporations in the province.

Form of Aid Provided

Term loans.

Criteria for Eligibility

Must create employment opportunities.

Financing must not be available on reasonable terms and conditions.

Expand markets for Manitoba products.

Encourage innovation in industrial enterprises.

Enhance efficiency and diversification of enterprises.

Terms of Repayment

According to ability to repay.

2. Manitoba Export Corporation

Purpose of the Program

To provide manufacturers assistance in marketing, shipping, tariff and foreign regulations and any other matters related to the exporting of products from Manitoba.

Form of Assistance Provided

Information concerning exporting and short term loans.

3. Manitoba Research and Development Grants

Purpose of the Program

To improve and introduce new products in Manitoba through research and developments.

Form of Aid Provided

Grants.

Criteria for Eligibility

Financial assistance must not be available from other sources.

4. Manitoba Design Improvements Assistance Program

Purpose of the Program

To aid companies to retain consultants in order to improve their competitive position.

Form of Aid Provided

Grants

Criteria for Eligibility

The produce must be manufactured in Manitoba.
Total expenditures to be paid by grant must not exceed $20,000 in any 2 year period.
Consulting in areas of market testing and evaluation, redesign of existing products and product planning and diversification.

5. Communities Economic Development Fund

Purpose of the Program

Loans for projects in remote and isolated areas of the province for the purpose of promoting economic development in communities with particular emphasis on economically disadvantaged people.

6. Manitoba Airport Assistance Program

Purpose of the Program

Grants and loans available to municipal airport commission responsible for the operation of airports in southern Manitoba which do not receive Class 1, 2 or 3 Commercial Air Services.

7. Manpower Development Assistance

Purpose of the Program

To carry out analyses to determine the productivity of the company's work force. To analyse policies and practices set up by the company to monitor manpower activity. To design, where necessary senior management, supervisory staff and production personnel training programs. To establish personnel models and management systems related to human resource development.

Form of Aid

The department will share with the firm in the costs of consultants to carry out approved programs on the following basis:

2/3 of the first $2,000.
1/2 of the next $3,000.
1/3 of the next $10,000.

8. Productivity Improvement Program

Purpose of the Program

Productivity audit analyses of individual firms and industry groups by industry specialists who will identify problem areas, obstacles to growth and opportunities for improvement in the marketing, production, technology, manpower, organizational effectiveness and financial areas of the firm and the provision of recommendations which are suited to the needs and capabilities of the firm and which include a blueprint for action.

9. Feasibility Studies Incentive Program

Purpose of the Program

To assist companies in the commissioning of feasibility studies to develop plans for establishing or expanding manufacturing facilities in Manitoba. To assist companies in making application to obtain grant assistance from the Federal Department of Regional Economic Expansion.

Form of Aid Provided

The cost of professional advice from private consulting and advisory sources used to assist in the feasibility study or in applying for Federal grants will be shared by the department on approved projects as follows:

2/3 of the first $2,000.
1/2 of the next $3,000.
1/3 of the next $10,000.

10. Work Activity Project

Purpose of the Program

Specific community areas in the province have been designated for financial assistance through local work activity committees. The funds are for training and materials but do not apply to direct capital investments.

ONTARIO

1. Ontario Development Corporation

Purpose of the Program

To provide financial and advisory services to business in order to stimulate industrial growth, economic development and employment opportunities in the province.

Form of Aid Provided

Performance loans and term loans.

Criteria for Eligibility

Operations must contribute to the economic development of Ontario.
Management must be capable and the venture must be financially sound.
Applicants must have sufficient equity in the business to warrant financial assistance.
Funds not available for primary industry.

Loans Programs Available

Performance Loans

a) Equalization of Industrial Opportunity Program
b) Fisheries Restructuring

Term Loans

a) Loans to small businesses
b) Venture Capital for Canadians
c) Pollution Control Equipment Loans
d) Tourist Industry Loans
e) Industrial Mortgages and Leaseback

Repayment Terms

Performance loans are interest free and conditional upon satisfactory performance, may be progressively forgiven over a six year period.
Term loans are at conventional interest rates and the terms are fitted to individual circumstances.

2. Export Support Program

Purpose of the Program

To provide assistance to Ontario based exporters encountering difficulties in financing exports of capital and consumer goods. This program is administered by the Ontario Development Corporation.

Form of Aid Provided

1. Short term financing of production of goods for export.
2. Short term financing of export goods held in warehouse.
3. Medium term export financing of capital goods.
4. Short term financing of consumer goods.

Criteria for Eligibility

1. Company must be Ontario based.
2. Unable to obtain the necessary export financing from E.D.C.
3. The goods must have a significant Canadian content.
4. Acceptable security must be available.

3. Business Development Services

Purpose of the Program

The Business Development Division of the Ontario Ministry of Industry and Tourism encourages the establishment of new job producing industries and the expansion of present manufacturing concerns throughout Ontario.

Organization

The programs are administered through 2 branches:

a) Industrial Development Branch
   i) industrial locations section
   ii) manufacturing arrangements section
   iii) technology section

b) Trade Development Branch
   i) international marketing section
   ii) design and engineering services section
   iii) marketing services section

4. Ontario Research Foundation

QUEBEC

1. An Act to Promote Industrial Development Through Fiscal Advantages

Purpose of the Program

To encourage the use of advanced technology to produce newly conceived products not yet manufactured in the province of Quebec.

Form of Aid Provided

Tax incentives whereby a company may deduct an amount equal to 30%, 50% or 100% of their annual investment according to whether it is made in Zone I, II, or III up to a total of $10,000,000 during the period April 1971 to March 31, 1974.

Criteria for Eligibility

1. Investment must exceed $150,000.
2. Every company which is engaged in the operation of a manufacturing or processing business.

2. Quebec Industrial Development Assistance Act

Purpose of the Program

To encourage manufacture of newly-conceived products, to consolidate a company's means of production while adapting them to modern techniques so as to increase their share of the market, and to provide financial assistance at reasonable rates to qualifying companies who cannot obtain financial assistance otherwise.

Form of Aid Provided

1. Loans secured by mortgage, machinery, etc. at current interest rates.
2. Leasing of machinery, tools or equipment.
3. Purchase of up to 30% of the equity of a company.
4. Grants.
5. Loan cost sharing.

Criteria for Eligibility

1. Competent management.
2. Must invest at least $150,000 in the Province of Quebec.

3. Financial Assistance Programs for Fast Growth Industries

Purpose of the Program

To promote the location or expansion in Quebec of established firms in fast growth industries who:

i) apply advanced technology,
ii) manufacture a product not previously manufactured in Quebec, and
iii) who are in a position to export.

Form of Aid Provided

Subsidy

Criteria For Eligibility

a) must locate in a slow growth area
b) will apply advanced technology or manufacture a product new to Quebec
c) will be able to export
d) projected investments exceed $5,000,000
e) must provide employment for residents of Quebec

4. The General Investment Corporation of Quebec

Purpose of the Program

To take an active part in the industrial development of Quebec.

Form of Aid Provided

Long term loans

5. Quebec Industrial Credit Bureau

Purpose of the Program

To promote the development of manufacturing industry in the province.

To aid small and medium sized industrial operations located in slow growth areas of Quebec which do not have access to usual financing sources.

Form of Aid Provided

Secured term loans

Criteria for Eligibility

Loans for the purpose of:

a) purchase of land and construction, improvement or expansion of plants or factories,
b) acquisition of machinery, tools and equipment,
c) improvement or consolidation of the firms financial structure,
d) must be located in Quebec, be engaged in manufacturing or processing and have good growth potential,
e) must locate in a slow growth region,
f) financial aid must not be otherwise available.

6. Regional Industrial Development Assistance Act

Purpose of the Program

To promote industries and the expansion of existing industries in the slow growth areas of Quebec.

Form of Aid Provided

Grants

Criteria for Eligibility

To manufacturing or processing firms for investments of at least $50,000 in regions designated by provincial authorities. Investments must be made in the construction or expansion of plants, purchase of machinery, tools or equipment.

Amount of money available

Varies according to location.

NEW BRUNSWICK

1. New Brunswick Development Corporation

Purpose of the Program

Assist in the expansion and diversification of existing industry and encourages new manufacturing and processing industries to locate and develop in New Brunswick.

Form of Aid Provided

Loans or guarantees of loans with first mortgage security.

Criteria for Eligibility

The funds must not be obtainable on reasonable terms from other sources.

Directed primarily to secondary manufacturing.

New companies wishing to establish in the province or existing companies requiring capital for expansion and/or introduction of more efficient equipment and methods.

2. New Brunswick Industrial Finance Board

Purpose of the Program

To provide financial assistance to certain types of new or expanding industries.

Form of Aid Provided

Direct or guaranteed loans.
Equity participation.
Assistance in plant location and technical advice.

Criteria for Eligibility

Available for recognized manufacturers to apply to land, buildings, machinery and equipment.
Funds must not be available from conventional sources on reasonable terms.
Applicants are expected to match dollar for dollar with the loan.

3. New Brunswick Guarantee Loan Board

Purpose of the Program

To guarantee bond issues and long term loans.

4. New Brunswick Research and Productivity Council

Purpose of the Program

To provide free technical information and industrial engineering services to firms in New Brunswick and Prince Edward Island. It operates under arrangement with the National Research Council.

5. Export Assistance Program

Identical to Program for Export Market Development administered by the Department of Industry, Trade and Commerce of the federal government. The provincial government provides additional assistance above that provided by the federal program.

6. New Brunswick Design Council

Purpose of the Program

To provide New Brunswick industry with a service of assessing products or prototypes by qualified experts, as an aid to increasing sales and/or reducing manufacturing and development costs.

Eligibility

A submission may be entered by any firm in the province of New Brunswick provided the item is made in New Brunswick and maximizes New Brunswick content.

7. New Brunswick Multiplex Corporation

Purpose of the Program

The Corporation was established by the federal and provincial governments to promote and implement a major project involving construction and operation of a number of interdependent metal-working plants in and around Saint John, New Brunswick.

8. Northeast Development Program

Purpose of the Program

A pilot program to encourage and assist the modernization, expansion and establishment of small industry.

Form of Aid Provided

The program is sponsored under the Northeastern F.R.E.D. Agreement with 75% of the cost borne by D.R.E.E. and the remainder by New Brunswick through the Community Improvement Corporation.

1. Forgivable Loans (D.R.E.E. formula).
   New equity in the amount of 20% of approved capital cost must be advanced prior to drawdown of funds under the forgivable loan.

Criteria for Eligibility

To be eligible a project must involve manufacturing or processing or a maintenance or repair facility related to the manufacturing sector.

NOVA SCOTIA

1. Industrial Estates Limited

Purpose of the Program

To promote the establishment of new industry and expansion of existing industry in Nova Scotia.

Form of Aid Provided

Loans. Will finance 100% of the cost of land and buildings, 60% of the installed cost of new machinery, including sales tax, duties, shipping and installation costs.

Criteria for Eligibility

Secondary manufacturers locating in Nova Scotia.

Repayment Terms

Flexible.

2. Industrial Loan Board

Purpose of the Program

To assist in the establishment, expansion and modernization of a variety of industrial and tourist enterprises.

Form of Aid Provided

Loans up to 75% of the current appraised value.
Loans must be secured.

Criteria for Eligibility

Manufacturing, processing industries or tourist industry;applicant must have reasonable equity.

3. Nova Scotia Bonus Act

Purpose of the Program

To provide an incentive for companies to locate in certain municipalities.

Form of Aid Provided

Reduction in municipal taxes charged to the company because of locating in designated municipalities.

4. Agriculture and Rural Credit Act

Purpose of the Program

To make loans to, or guarantee loans of, a borrower for the purpose of acquiring or improving any farm, plant, machinery, or equipment.

Form of Aid Provided

Loans and guarantees.

5. Fisherman's Loan Act

Similar to Agriculture and Rural Credit Act in purpose, with orientation specifically to the fishing industry.

6. Industrial Development Act

Purpose of the Program

To establish, assist, develop and expand industries in the province.

Form of Aid Provided

Assistance by way of loan, loan guarantee, bonds, and acquisition of equity.

7. Forest Improvement Act

Form of Aid Provided

Loans for the purchase of forest lands up to the maximum amount of $100,000.

Criteria for Eligibility

Have been efficiently operating an established forest product mill.

8. Nova Scotia Resources Development Act

Purpose of the Program

To aid, assist and promote the development of resource-based industries, businesses and activities within the province.

PRINCE EDWARD ISLAND

1. Prince Edward Island Provincial Department of Labour, Industry and Commerce

(a) The Business Services Unit

Provides free consulting services to local industries in specialized areas such as plant layout, product design, new product development, quality control and financial management.

(b) The Industrial Development Unit

Attracts new industry to P. E. I. and assists in expanding existing industries by providing free feasibility studies and assistance in obtaining financing.

2. Prince Edward Island Lending Authority

Purpose of the Program

To assist manufacturers, processors, farmers, fishermen and operators of tourist establishments to obtain operating capital as well as medium term loans.

Mainly aimed at providing working capital to small business.

Form of Aid Provided

1) Guaranteeing loans
2) Term loans

Criteria for Eligibility

The operation must contribute to the economy of Prince Edward Island.

3. Prince Edward Island Industrial Enterprises Incorporated

Purpose of the Program

To provide assistance to industries wishing to establish or expand their facilities.

Form of Aid Provided

Direct loans or loan guarantees.
Security required.

4. Prince Edward Island Market Development Centre

Purpose of the Program

a) to collect and provide information for those with immediate marketing problems.

b) to set up facilities to develop, test and complete market analysis for new products.

c) to initiate studies to identify future changes needed in marketing.

d) to establish contacts in various industries, research groups and government agencies to facilitate improved communications and cooperation.

e) to collect information on foreign markets and review market research performed elsewhere.

f) to assist in providing promotion through product design, packaging, advertising, distribution and test marketing.

g) to assist in improving the quality of existing product lines.

The assistance is provided free by the government.

NEWFOUNDLAND

1. Newfoundland and Labrador Development Corporation

Purpose of the Program

To provide financial assistance to qualifying businesses wishing to expand, modernize or locate in Newfoundland.

Type of Aid Provided

Direct loans or loan guarantees.

2. Department of Rural Development

CHAPTER V

CONCLUSIONS AND RECOMMENDATIONS

Summary

The primary objective of this study was to determine the availability of venture capital in Canada and in Ontario in particular. We examined the assembly and allocation by private and public intermediaries and the implications for public sector policy. The study investigated both the supplier and user sides of the issue, concentrating on the terms under which such capital was available, from whom it was available and for what types of investment.

Other objectives of the study included an investigation of the role of Canada's major financial institutions in the provision of venture capital and the effects of government regulation, including tax, on their provision of such capital.

The final phase involved a study of the various federal and provincial government industrial assistance programs. The emphasis here was on the applicability of these programs to small business. Special attention was given to the provincial government programs.

The main conclusions of this report are:

1. Many ventures in Canada are worthwhile financing, but currently cannot obtain it. This is especially true for firms during the first few years of their lives when capital for startup and development is not available. The capital which is provided for the startup of new businesses in Canada is typically provided by groups of individuals. There is no formal process whereby entrepreneur and investor can get together for this type of financing.

2. There is insufficient venture capital available for the start-up and development phases of new firms in Canada. Most of the venture capital available is directed into the expansion of established companies or acquiring existing companies. In addition, there are fairly tight restrictions, both on the type of investment and its geographical location, which prevent firms in certain industries (e.g. service industries) and areas (e.g. Northern Ontario) from obtaining venture capital. The terms under which this capital is available are often viewed as being prohibitively expensive by the user, either in terms of the debt load or the amount of equity the firm must surrender.

3. There is a distinct lack of venture management ability in Canada. Managers of venture capital firms claim that poor management is the prime reason for rejecting most of the proposals they examine.

4. Government programs do not provide venture capital as we have defined it. Equity financing is rarely involved and most of the debt is fully secured. However, in areas like Northern Ontario, government aid is the only form of capital available to many small businesses and they consider it to be venture capital.

5. Government regulations and tax laws do not prevent financial institutions from becoming more involved in the provision of venture capital in general. There are several notable exceptions, however. Institutions are the prime source of new capital entering the area of venture capital investments.

6. Foreign firms and individuals are not a significant source of funds for venture capital companies in Canada. However, many user firms are forced to seek funds in the United States, especially during the early stages of their development, when such capital cannot be obtained in Canada. This higher risk capital is more easily found in the U.S. because of differences in tax laws regarding the writeoff of losses and the greater availability of capital in the U.S. This is especially true of the natural resource industries such as oil and gas.

7. The amount of venture capital in Canada is expanding, especially considering the recent activity of the Canada Development Corporation. But it is not changing

its focus towards younger firms. On the other hand, the demand for venture capital has increased rapidly, as evidenced by the growth in the number of potential investments examined each year by venture capital companies.

8. Current tax legislation does not provide individuals nor corporations sufficient incentive to invest in higher risk investments such as young companies or natural resource exploration. U.S. investors have greater incentives through more liberal loss write-offs, for example.

9. Current taxation of venture capital firms on an income basis rather than at capital gains rates has influenced some venture capital firms to change their focus. Some of them are moving towards a holding company approach, whereby they acquire equity control of their investments and operate the firms as subsidiaries. They are then not in the venture capital business and would presumably be taxed at capital gains rates when they sell their investments.

The main recommendations for government resulting from the study were that:

1. The government should establish a "clearing house" whereby users could learn of venture capital sources and their preferences and venture capital sources could locate worthwhile ventures. This center would also provide assistance in preparing and evaluating proposals.

2. The government should provide incentives to attract more private capital into venture capital investments, especially at the start-up level. The most appropriate suggestion was the establishing of Small Business Investment Companies similar to those found in the U.S. with the capability of raising funds from the public and from financial institutions in Canada. These firms could either borrow directly from the government or use government guarantees to raise funds via public security issues.

3. Government programs like the Ontario Development Corporation do not currently have the personnel skilled in making equity investments. One way for the ODC to make equity investments in small firms is to participate in joint ventures with private sources of venture capital. These investments could then be managed by venture capital firms in the same manner as they are currently managed for financial institutions.

This is a possibility while the concept of SBIC's proposed above is being investigated and may be the best eventual form of an SBIC program for Canada.

4. Current taxation policies should be changed to give individuals and firms more incentive to invest in high risk ventures, especially at the start-up and development level. This should be primarily through more liberal loss writeoffs to decrease the risk of venture investments.

5. Provincial and federal governments should co-operate as suggested below on planning assistance for small businesses. Any move towards a program similar to the SBIC program should be planned jointly. This should be done by having the Federal Department of Industry, Trade and Commerce and each Provincial Department of Commerce establish a Small Business Development Agency. These agencies could then jointly plan to assist small businesses in Canada.

6. These agencies could administer the "clearing house" suggested earlier and arrange for courses through our universities and community colleges aimed at the small businessmen.

It is suggested that the Ontario government's role in implementing these recommendations should be to sponsor a joint federal-provincial conference on the problems of small business. It should then propose these recommendations on a cooperative basis with the other levels of government.

Availability of Venture Capital

We conclude that there is insufficient venture capital available in Canada for the start-up and development phases of new businesses. This is the period during the first few years of a firm's life cycle when collateral is lacking, sales are low and profits are often non-existent or negative. The replies from our user survey unanimously agreed that this was the most difficult stage for most firms to raise financing. This is an important distinction from the Gray Report conclusion. There was also a consensus among users that the major weakness of the user firms surveyed was lack of capital.

Although one author claims that there is an excess of venture capital available in Canada waiting for appropriate investment,[1] this capital is not primarily available for new ventures. It is mainly available for the expansion of established companies and there is a definite lack of venture capital for firms during the first few years of their existence. Currently start-up capital in Canada is primarily invested by small groups of individuals. The entrepreneur requires some means of locating these investors interested in financing a start-up.

In addition, the capital is available primarily for high technology oriented ventures and for firms with a great potential for export. Therefore, most service industries in Canada do not have access to such capital.

Firms which are not located in the Toronto, Montreal and Vancouver areas have little chance of finding funds for any type of venture. In fact, the entrepreneurs in the Toronto area have a definite geographical advantage over other

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[1]"The Problem with Venture Capital is the Courtship". D. Rumball, Financial Post, June 30, 1973.

users in raising venture capital.[1]

Venture capital firms usually insist on acquiring some debt as well as equity from the borrowing firm, although the debt may be convertible into equity. Government programs provide only loans or grants. The small firm, usually heavily debt financed before approaching a venture capitalist or government program, often does not have the capacity to absorb more debt. It is equity that small firms need and it is our conclusion that there is insufficient equity financing available to small businesses in Canada, especially during the early years.

But the limited availability of suppliers of equity capital to small firms coupled with the high demand for such capital means the price will be high. Any action by government to increase the supply of both debt and equity capital to small businesses would decrease the cost which small businesses must pay.

Lack of Venture Management

The greatest weakness of small firms in Canada, expressed by venture capital suppliers, government officials and, to some degree, by small businessmen themselves, is the lack of capable management. Canadian managers are often not capable of preparing a reasonable presentation to obtain funds. This is one reason that many Canadian venture capital

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[1] "Venture Capital Easier to Raise in Toronto," Toronto Globe and Mail, May 8, 1973.

firms prefer to invest in ventures located in the United States.

A recent series of seminars given by a venture capital firm in various cities across Canada attempted to improve this proposal deficiency problem. This course suggests how to approach venture capital firms, what a proposal should contain and general advice for obtaining government aid, as well. However, the attendance at this seminar has included more intermediaries (accountants, bankers, lawyers), than small businessmen, perhaps because the latter could not afford the time and expense of the seminar.

One additional problem encountered among the user firms is that entrepreneurs are often unwilling to surrender equity. This is especially true when the entrepreneur believes that the venture capitalist is demanding too much equity for his funds. This usually results from the fact that an entrepreneur is very optimistic about his firm's value while the venture capitalist tends to be pessimistic. The entrepreneur may not be capable of correctly assessing the risks involved in his firm, especially his own ability to manage his firm.

Government Programs

Government grant and loan programs, both provincial and federal, do not fall within our definition of venture capital. The debt offered by these programs is fully secured and equity is rarely involved in government financial aid.

Government grants could be considered as venture capital, but few small firms qualify for them.

Government aid is limited to a narrow range of firms in most cases, usually high technology firms involved in research and development and capital intensive manufacturing firms. Service firms qualify for little government financing.

Officials of government programs are cautious in their evaluation of companies and will seldom invest in a firm with no profitable history or "track record". The firm must have the capacity to carry the additional debt load imposed by the government loan and the ability to repay it. Many small firms cannot support additional debt.

In the more rural areas of Canada, such as Northern Ontario, government programs are often the only source of financing available to small firms. Firms in these areas certainly view government programs as venture capital.

Government Regulations

The legislation governing the various Canadian financial institutions does not prevent these firms from participating in the provision of venture capital. The institutions normally participate as second level investors, by investing in a venture capital company rather than supplying capital directly. Those firms which have invested directly usually find they do not have the management expertise to evaluate and monitor ventures and then revert to investing via a venture capital firm. A relatively new form of venture capital company is the "packager", which syndicates ventures among financial institutions, individuals and industrial firms. Using this approach, the investors can select those ventures they desire to invest in and reject those they dislike. The "packager" will invest a small portion of the funds and will do the evaluation and monitoring for a fee. Government programs could also invest equity in joint ventures in the same way as the financial institutions, with venture capital firms performing the evaluation and monitoring function.

Certain major financial institutions like life insurance companies make venture capital investments under their "basket clauses", since these ventures are ineligible investments for them, except under these clauses.

Foreign Capital

Foreign sources of funds do not participate to any degree in Canadian venture capital companies. But many users of venture capital are forced to approach American sources to obtain the funds they need. This often results in a loss of control of the firm to American interests and these firms often eventually become subsidiaries of American companies. In addition, many small firms are sold to foreign investors after attempts to raise funds in Canada have failed. Examples of this were encountered among the user firms surveyed in Chapter II.

American capital is more easily available during the early stages of growth of a small firm and for types of ventures which Canadian firms do not prefer, such as natural resources.

The Amount of Venture Capital

The total volume of venture capital available in Canada has grown rapidly since about 1969, especially with the funds supplied by the Canada Development Corporation. Sources confirm that there is a large amount ($30 million dollars in Toronto alone) of venture capital available for investment in June of 1973, because venture capital sources cannot find ventures which they consider worthwhile.

It is our opinion that this capital is uninvested because the terms under which it is available are too restrictive, both in financial cost and types of investment for which it is available. This capital is not available for firms at the start-up or development stage, nor service firms in general nor for firms in rural areas of Canada.

An example of this problem is a venture capital firm which, after being established one year ago, has not yet made a single investment. It has a total of $5 million to invest. But this capital is limited to a narrow range of high technology products and is not available for new firms.

Much of the venture capital in Canada is invested already in the United States and Canadian suppliers are actively seeking investment opportunities in the U.S. Few American companies come to Canada seeking venture capital, so the Canadian suppliers seek ventures there.

Tax Effects

Canada's tax legislation does not provide sufficient incentive to individuals or firms to invest in high-risk, relatively new ventures. American investors have much greater incentive through more liberal loss writeoffs, for example.

In addition, Canadian venture capital firms are complaining that they are being forced to become holding companies which control and operate their ventures. This, they claim, is because they are being taxed as investment companies (at income rates) rather than at capital gains rates. Since they are in the business of investing, the government treats them as investment corporations under Section 130 of the Income Tax Act. But these firms claim they are not covered by this section since their participation in these firms is not really marketable and they hold relatively large shares of relatively few firms for long periods of time.

If these firms do become holding companies, they will limit their investments even more to companies in which they can buy equity control and manage or operate afterward. This will further restrict the availability of venture capital in Canada.

Provincial corporate taxes, including that of Ontario, are typically based on the federal tax classification. Therefore, venture capital firms in Ontario are subject to the provincial 12% income tax as well when they are taxed federally based on income rather than capital gains.

Recommendations for Government Action

The main implications for government action at both the federal and Ontario level are stated in this section. It is our opinion that there is some unnecessary duplication of assistance programs at the federal and provincial levels. We therefore recommend that both the Ontario government and the federal government should establish a Small Business Administration or Agency for liaison with small firms, administration of small business programs and liaison between the federal and provincial levels on small business assistance.

A Small Business Clearing House

The Ontario government should encourage the federal agency to include a "clearing house" as part of its agency, where users could obtain information and advice. This center would also serve venture capitalists, especially individuals and small groups, in allowing them to review proposals on file. No mechanism currently exists for individuals to invest in venture capital situations other than as random opportunities arise. This approach would permit the financing of new ventures by syndicates of individuals, venture capital firms and financial institutions.

This center should also provide counselling assistance to small businessmen on preparing proposals and should offer courses on the elements of operating a small business. It could also administer other programs aimed at small firms.

SBIC's for Canada

The Ontario government should cooperate with the federal government in the creation of Small Business Investment Companies operating under charters from the Small Business Agencies recommended above. These firms would be incorporated by private individuals and financial institutions who would collectively provide a minimum equity participation of say $1,000,000 to obtain a charter as a SBIC. This charter would permit the firm to raise capital by the issue of government guaranteed debentures on the Canadian capital markets. The government guarantees would permit Canadian financial institutions to invest in these debentures. If the interest offered on these debentures was slightly higher than that on government bonds, funds would be channelled into these SBIC's.

However, the terms under which these SBIC's would be permitted to operate must be strictly controlled. In the American situation, much of the funds was channelled into real estate and various other non-venture investments. For Canada, the capital should be restricted to new and young firms in primarily manufacturing, service and natural resource development.

For areas where the government desires regional development, such as in Northern Ontario, the SBIC's investing there could be permitted to leverage their equity base more than the normal amount using the government guaranteed debentures. The standard SBIC would be permitted to leverage its equity by issuing, say, three times as much debt (to a maximum of $3 million), SBIC's specializing in certain areas, such as Northern Ontario, would be permitted to leverage its equity base to a 5 to 1 maximum ratio; or $5 million in debt. It is recommended that the provincial government should guarantee this additional $2 million, while the federal government guarantees the original $ 3 million. Each province could then decide the maximum level to which firms operating in that province or portions of it could be leveraged.

One form of an SBIC is similar to the "packager" venture capital firm discussed earlier. Those firms licensed as SBIC's could approach existing government programs such as the ODC for funds as they do financial institutions. The ODC, for example, could then decide whether it would invest. This arrangement would most likely involve equity participation by these government programs. But the SBIC could perform the management function of that equity investment.

Another possible form of SBIC for Canada is one where the SBIC, once licensed, is essentially free of government involvement. The firm issues debentures to the public which are guaranteed by the government up to specified multiples of the firm's equity base.

Since the SBIC program in the U.S. had extensive problems during its early years, an investigation of these problems and their implications for a Canadian SBIC should be undertaken. The objective of this study should be to examine the American program, design a similar program for Canada and recommend a procedure for initiating and operating such a program. This would include the design of criteria for issuing charters, terms of reference for the SBIC's and regulations for the operation of such firms. We intend to submit a proposal for such a study to the Ontario government.

Taxation Incentives

Both the federal and provincial levels of government should investigate possible changes in tax legislation to attract more private capital into high risk ventures. A more liberal method of writing off losses on venture capital investments would be the most appropriate in our opinion. The federal government should also examine the taxation of venture capital firms, since the current income taxation of the investments is forcing these firms out of the venture capital area in the acquisition field.

Any liberalization of the tax regulations should be aimed at channelling more funds into new and relatively young businesses. This is where capital is currently very scarce.

These are the main recommendations from this study. The lead in implementing these must be undertaken at the federal level, with the provinces cooperating on issues of special concern to them. The role which the Ontario government should play immediately is to encourage the federal and other provincial governments to implement the above recommendations.

One method of bringing the Ontario government's concern for small business to the attention of the other levels of government is for it to propose a joint federal-provincial conference on the topic. This conference could be hosted by the Province of Ontario and the recommendations of this and other studies could be discussed jointly. This cooperative approach in attacking the problems of small businessmen in Canada would minimize the proliferation and duplication of assistance programs.

UNIVERSITY GRANT PROGRAM RESEARCH REPORTS

RAPPORT DE RECHERCHE SUR LE PROGRAMME DE SUBVENTIONS AUX UNIVERSITES

	AUTHOR(S)/AUTEUR(S)	UNIVERSITY/UNIVERSITÉ	REPORT TITLE/TITRE DE L'OUVRAGE
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