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Southern Interior Development Initiative Trust

A Report Prepared for the Ministry of Jobs, Trade and Technology
Province of British Columbia

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Report on the Operations of the Southern Interior Development Initiative Trust

1. Introduction

The Ministry of Jobs, Trade and Technology engaged Simplex Management Consulting Ltd. to conduct a fact-finding review of the operations of the Southern Interior Development Initiative Trust (SIDIT) in order to:

- Provide the Province with a complete and balanced view of their operations;
- Prepare a report regarding the current operations of SIDIT; and
- Make recommendations on the future strategic direction in support of the core objectives of SIDIT: optimum contribution to the economic development and diversification of the region, and to ensure the long-term sustainability of the trust.

CAVEAT: A key part of the review was to delve into individual loan files to determine if the new loan procedures were being complied with and to determine if alternative approaches to litigation would be appropriate to manage a given loan file. However, SIDIT did not grant access to loan files citing client privacy and a requirement to obtain client approvals, despite the offer to sign a non-disclosure agreement. As a result, observations and recommendations in this report are limited and solely based on conversations with Board members, staff and a review of publicly available SIDIT documents.

The report includes observations on the operational infrastructure needed to support this direction and any other matters deemed important, subject to the caveat above. In addition, this review does not include any assessment as to whether SIDIT is in compliance with Section 22 of the *Act*. (*Sec 22 – Investments* - The Southern Interior Development Initiative Trust must invest the Southern Interior one-time development allocation, and any other money in the Regional Account, only as permitted under the provisions of the *Trustee Act* respecting the investment of trust property by a trustee.)

The report is written for and presented to the Ministry. It is assumed the report will be forwarded to SIDIT with the understanding they are under no obligation to consider any of the recommendations.

This report has been developed based on two methods of information collection. First, through the review of publically available documents created by SIDIT and others (see Appendix 1 for a list of public documents reviewed). Second, through conversations with SIDIT Board members and staff, who volunteered to engage in conversations to provide input into this report, as well as Ministry staff. The information gathering took place during the period October 10, 2018 to November 6, 2018. The author thanks and is very

appreciative of the Board members and staff who provided invaluable insight for the creation of this report.

2. Background

On February 27, 2006, the Government of British Columbia established SIDIT through the *Southern Interior Development Initiative Trust Act* and a one-time payment of \$50 million. The objective of SIDIT is to assist in the growth and diversity of the economy of the Southern Interior of British Columbia. Part 4, Section 20(1) of the *Act* identifies ten critical sectors in the Southern Interior that the Trust can invest in:

- Forestry;
- Pine beetle recovery;
- Transportation;
- Tourism;
- Mining;
- Olympic opportunities;
- Small business;
- Economic development;
- Energy; and
- Agriculture.

SIDIT is governed by a Board of Directors of thirteen individuals. Eight members are appointed from the two Regional Advisory Committees (RACs), and five are appointed by the provincial government. The RAC members are local government elected officials and MLAs from the region.

The *Act* establishes SIDIT as a corporation with the powers and capacities of an individual of full capacity. Also, the *Act* states that SIDIT is not an agent of the government. This means SIDIT is an independent corporation and does not report to, nor take direction from, government. However, there is an entire Part to the *Act* which outlines the Board's Public Accountability responsibilities. The Board of Directors is solely responsible for compliance with the *Act*, delivering on their strategic plan, and operating the corporation.

The current staff complement is four plus one contractor. The staff positions are:

- Acting Chief Executive Officer
- Chief Financial Officer
- Director of Loans/Corporate Governance
- Portfolio Manager (contractor)
- Loan Portfolio Administrator

(Note: The Chief Financial Officer is also the Acting Chief Executive Officer)

3. Discussion

SIDIT's objective is to assist in the growth and diversity of the economy of the Southern Interior of British Columbia. This is identified in SIDIT's Fiscal Year 2019-2021 Strategic Plan. The Plan is a comprehensive roadmap designed to satisfy the objective of growing and diversifying the Southern Interior economy. Job creation and job maintenance is a cornerstone of the Plan.

The SIDIT Board of Directors share a vision of the future for the Southern Interior. That **vision** is:

- A future where economic opportunities are enabled, providing long-lasting measurable benefits to communities.
- A future where regional investment creates significant positive impacts across the region and smaller communities are given opportunities to remain or become economically sustainable.
- A future where there is a strong and diversified economy in the Southern Interior that supports the development of viable, healthy, vital and sustainable communities throughout the region.

The **mission** of SIDIT is to support strategic investments in economic development projects that will have long-lasting and measurable benefits in the Southern Interior.

An essential section of the current strategic plan is Section VI – Strategic Goals:

SIDIT's goal is to maintain the Trust so that it is sustainable, increasing the value of the Trust over time and achieving the Trust's desired ends within available means. As part of the Strategic Goals, the Board established a core strategy supported by five strategic goals. The core strategy is:

- Identify and support community development projects and regionally based commercial ventures that match the objectives of the Trust and demonstrate sustainability.
- Maintain the Trust so that it is financially sustainable, providing continual support for economic initiatives for the Southern Interior and increase the social and economic impact of the Trust over time.
- Supporting each of SIDIT's five strategic goals are strategies, performance targets and metrics that track progress and measure goal achievement.

The five strategic goals are:

- Goal 1: Enhance the Southern Interior economy by promoting greater economic growth, resiliency and diversification.

- Goal 2: Preserve existing jobs, stimulate new employment and address skill shortages in the Southern Interior region.
- Goal 3: Attract new capital to the Southern Interior region to drive incremental economic development activities.
- Goal 4: Increase the value of the investment pool, thereby increasing opportunities to support regionally strategic investments in the Southern Interior.
- Goal 5: Create and sustain public awareness of and support for the Trust's purpose, goals, achievements and successes with a focus on partnership development, collaboration and extending rural reach.

Each goal has several accompanying strategies to ensure success of the goal.

The Core Strategy is fundamental to SIDIT going forward. ^{s.13} Given the constraint of a finite annual income stream, they must weigh supporting the community and businesses and at the same time ensure the long-term financial viability of SIDIT. The Board fully understands this and is committed to the core strategy.

4. SIDIT Operations

The parameters for the content of the report include a review of the operations of SIDIT as at October 2018. Operations of any company include accounting, payroll, accounts receivable, accounts payable, policy and procedures, etc. For SIDIT, these financial and administrative functions are performed well. Staff is paid, funds are received, suppliers are paid, and the books of account are maintained appropriately as evidenced by an unqualified audit opinion from the inception of the organization.

Although the financial and administrative functions of an organization are important, the critical focus of this report is the loans and equity investments portfolio, how it is managed and how effective SIDIT has been in engaging key stakeholders. A well-managed loan and equity investment portfolio and an effectively implemented communications strategy are essential to allow SIDIT to achieve its Core Strategy.

5. Annual Investment Income

SIDIT's first Board of Directors recognized that investing the initial \$50 million capital received from the Province in fixed income and share equities may not provide the consistent annual investment income required to provide grants to communities and businesses. In addition, providing grants to businesses is not a sustainable tool to drive economic development. Thus, an investment strategy which included loans and equity investments as well as fixed income and share equities was adopted. Subsequent Boards including the current Board have endorsed and maintained this approach.

6. Loans and Equity Investment Portfolio

The loan and equity investment portfolio is a critical component to the success of SIDIT. To date, SIDIT has issued \$49 million in loans and equity investments and has received \$29 million in principal and interest repayments. As at March 31, 2018, the loan portfolio totalled \$34 million s.13

7. Lending Framework

Organizations that adopt a loan and equity investment strategy accept the associated risk. SIDIT's Lending and Portfolio Procedures and Guidelines (updated March 22, 2018) states they will take an approach to commercial lending that is between conservative and moderately risky, with considerable emphasis placed on the integrity and management skills of the business operators. s.13,s.17

s.13,s.17

A vital component of a company's management of loan risk is the skills and experience of the staff or contracted resources that oversee the portfolio. SIDIT currently has a contracted resource that has exceptional expertise in loan and equity investment management. s.13

s.13

SIDIT define themselves as a gap lender. SIDIT partners with commercial banks, the Business Development Bank of Canada, and credit unions to fill the funding gap for clients s.13

s.13

Until recently, SIDIT has taken a different approach to lending compared to a traditional lending institution. SIDIT has been a patient lender. This means SIDIT has worked with loan and equity investment clients in an ideal world to negotiate terms that are reasonable to the client and SIDIT, to ensure a successful business partnership. This includes higher interest rates and longer periods of payment deferral in some cases than those the banks may offer. Higher risk with the potential of higher reward is the basic principle.

The Board is tasked with approving loans and equity investments. Documentation supporting the funding request must be sufficient and appropriate to enable the Board to make an informed decision. Information gathered from Board members' discussions indicate the documentation currently presented is relevant and comprehensive allowing for an informed decision.

s.13

8. Loan and Equity Investments Repayment

When a client receives a loan or equity investment, terms and conditions are agreed to by both parties in a legally binding document. s.13,s.17

s.13,s.17

Unfortunately, not all clients are successful in repaying their loan, despite their passion, effort and management expertise. SIDIT must turn to the loan or equity investment agreement to pursue legal avenues to recoup funds owing. This process is key to the Core Strategy of financial sustainability.

s.13 monitoring of the loan portfolio and increased communications with clients would enable SIDIT to respond in a timely fashion to support the business' expansion plans and/or in some cases take action under its loan agreement to avoid or reduce a loss.

9. Communication

A key component of any organization is communication. How the organization communicates both internally and externally cannot be underestimated. Good external communications with stakeholders, clients and the public drives business growth and generates meaningful partnerships. SIDIT, only infrequently, has undertaken external communications to advise the community on who SIDIT is, and how SIDIT can assist the community and businesses.

Of note, in the *Act*, Regional Advisory Committees (RACs) are referred to take an active role in the appointment of directors and to identify projects for the Board to consider. It appears that SIDIT has not maintained effective communications with members of the RACs as outlined in the *Act*. SIDIT staff indicate they are not responsible for setting RAC meetings and that RACs meet infrequently.

Communications with government staff is also very important. As indicated earlier, SIDIT is not an agent of the government and makes its own decisions. This, however, does not mean that communication between SIDIT and government staff should not occur. Some citizens consider SIDIT a quasi-government organization and, as SIDIT was created through legislation and funded through taxpayers, the Minister and Ministry

officials do have a responsibility to respond to concerns and enquiries. In discussions with SIDIT Board members, staff and government officials, a level of communication has been ongoing for many years. Having government officials knowledgeable about SIDIT and its current activities is good for all involved.

10. Summary of Observations

The report has so far focused on what the author believes to currently be the most important area of SIDIT, which is the loan and equity investment portfolio and its link to the financial sustainability of the organization. In addition, there are many other areas of SIDIT that have been observed or discussed with Board members and/or staff, or that were identified in the public documents, that will be highlighted in this section. The following key observations are described below:

A. The Vision

Board members provided an unwavering view that the vision for SIDIT was the appropriate vision reflecting the needs and aspirations of the region.

B. Important Financial Facts

From inception, SIDIT has provided valuable funding support to communities and businesses in the region. Funding has been used for student scholarships, grants to communities, and loans and equity investments to business. The following two tables summarize key information about SIDIT's use of financial resources in the region as at March 31, 2018 (2018 Annual Report).

Table 1

Financial Resources into the Region	\$ Millions	# of Jobs
Loans/Investments	49	
Scholarships and Grants	12	
Total Financial Resources	61	
Total Assets	48.3	
Total Principal and Interest Repaid	29	
Jobs Created and Preserved		3,392

Table 1 shows SIDIT has provided the region with \$61 million in financial resources via grants, scholarships, loans and equity investments since inception in 2006. These funds have helped communities with projects and assisted businesses to preserve and create new jobs totaling 3,392 or approximately 5 jobs per week. In addition, SIDIT has provided these financial resources to the region while maintaining an asset base of \$48.3 million, close to the original \$50 million provided from the Province.

Table 2

Loan and Equity Investment Portfolio	\$ Millions
Loans and equity investments outstanding	\$34.4
Loan provision	s.13,s.17
Loans written-off	17

s.13,s.17

C. Policies and Guidelines

Lending money or making an equity investment in a company introduces a certain level of risk to an organization. One way organizations mitigate this risk is by having very sound lending and equity investment policies, and loan administration procedures and guidelines. SIDIT has recently updated its Lending and Equity Investment Policy and their Lending and Portfolio Procedures and Guidelines (latest update, March 22, 2018), in response to identified weaknesses in the previous policy and guidelines.

The amended policy and guidelines provide the Board with more authority and oversight to approve material changes to the loan and equity investment agreements. Non material amendments approved at the CEO level are reported out at the next Board meeting. In addition, loan applicants must now read the Lending and Portfolio Procedures and Guidelines prior to completing their application. SIDIT also has the auditors review all new loans and equity investments to ensure they are in compliance with the policy and procedures. Staff indicated that prior to the March 22, 2018 amendments, material changes to loan terms were, on occasion, actioned after the Board had approved the loan terms. It is assumed this type of activity will stop with the new procedures.

The amended policy and guidelines documents provide SIDIT with very comprehensive loan and equity investment approval processes and ongoing oversight and management of the loan and equity investment portfolio. In addition, the quality of supporting documentation for loans and equity investments presented to the Board for decision is good, which indicates thorough due diligence has been undertaken.

However, applying the amended policy and guidelines to the existing portfolio has caused great concern from some clients of SIDIT as expressed directly to the Board of Directors, staff, government representatives and other economic development practitioners in the region.

D. Administration Costs

In SIDIT's first Annual Report, the Board chair discussed the minimization of administrative costs and stated, "resources be put to the highest and best possible use and that resources not be squandered on administration or excess overhead". SIDIT has continued with this theme of minimizing administrative costs. This is a good practice

for any organization so that the greatest percentage of funds can be employed to achieve their objectives.

E. SIDIT Chief Executive Officer Position

Over a period of 15 months in 2017 and 2018, SIDIT has undergone two leadership changes of the Chief Executive Officer (CEO) position. The CEO role is currently filled on an acting basis by the CFO. Having long-term stability in the CEO position is important to any organization. It instills confidence at the Board and staff levels, as well as from stakeholder and client perspectives. In addition, for SIDIT, the role is essential to implement the Strategic Plan which is a key responsibility of the CEO.

F. Overall General Observation

The SIDIT Board and staff have a true passion and unwavering desire for their organization to succeed and add value to the region through job creation and preservation. However, much greater attention needs to be paid to ensuring effective communications with clients, stakeholders and other interested parties in the region, particularly at a time where there has been a change in direction in its lending and collection criteria.

11. Recommendations

These recommendations are based on information collected through interviews or publicly available documents and are limited by the constraints in the caveat. Also, these recommendations are subject to the purpose in Sec 20 of the Act. (Sec 20 – purpose of the regional account is to support investment in the Southern Interior area).

A. Loan Repayment Policies

SIDIT undertook a comprehensive review of all policies in September 2017 and made appropriate changes where necessary, adopting these in March 2018. This review has resulted in a good suite of corporate policies. s.13

s.13

It is recommended that SIDIT undertake an immediate review of its complete portfolio and assess the current allowance for doubtful accounts.

SIDIT has recently formalized its lending and collecting procedures and guidelines, however care should be taken to ensure active monitoring of clients and their loans to ensure timely action should circumstances warrant.

B. Support to the Regional Advisory Committees (RACs)

The *Act* outlines a vital set of roles and responsibilities for the RACs in nominating eight (8) of the Board's 13 members, removing and replacing Board members and by providing advice on projects for the Board's consideration. In order for the RACs to support the activities of SIDIT, the policies and procedures of the RACs need to be clear and effectively communicated to RAC members. SIDIT can take the lead and provide operational support to the RACs. Currently, SIDIT staff indicate they are not responsible for providing this operational support.

The Act stipulates that the RACs are responsible for establishing their own procedures; s.13 between SIDIT and the RACs on whom SIDIT is dependent for its ongoing operation, it is recommended that SIDIT become much more active in supporting the operations of the RACs.

C. Staffing

i. CEO

SIDIT is an organization with a very small staff complement. The CEO position is currently filled on an acting basis. The CEO must possess the skillset necessary to deliver on the Strategic Plan the Board has created, which is robust. Having one individual as both CEO/CFO deliver on this Plan could compromise the effectiveness of both positions.

Although the Act indicates the CEO and CFO may be the same individual, it is recommended SIDIT hire a stand-alone CEO.

ii. Loan and Equity Investment Officer – Permanent Position

SIDIT currently has one contracted resource to assist in managing the loan and equity investments portfolio.

It is recommended SIDIT consider creating a permanent Loan and Equity Investment Officer position. Although the current contractor has vast experience in this area, a permanent employee undertaking the loan and equity investment oversight would be more desirable and provide stability for the organization.

D. Communications

The frequency and content of communications, particularly recently, between SIDIT and its clients, stakeholders and economic development officials s.13

s.13

It is recommended that SIDIT develop a comprehensive plan to clearly communicate its strategies, direction and approaches to its stakeholders. It is also recommended to explore the possibility of establishing a high-level communications protocol which will set a framework between SIDIT and provincial officials.

E. Economic Diversification

i. New sectors

Goal 3 of the fiscal 2019-2021 Strategic Plan is to attract new capital into the Southern Interior region. To attract new capital, one can look to existing traditional sectors to achieve this goal. Another approach is to look to new/emerging sectors, such as s.13

ii. Business Ownership

SIDIT currently provides funding to businesses as equity investments and receives common or preferred shares. SIDIT does not have any input into how the company is operated and does not participate in decision making. s.13

s.13

iii. Diversified Lending Model

SIDIT is a gap lender. s.13,s.17 . If the loan is performing well, SIDIT receives its principal and interest. However, should the client default, recovering funds is difficult and not always successful.

s.13,s.17

F. Regional Impact

Below are two tables from the SIDIT 2018 Annual Report. The first shows loan funding by region and per capita. The second shows grant funding by region and per capita.

Table 3 - Loan Funding by Region and Per Capita

Regions	2018	Cumulative	Population	\$ Per Capita
Central Okanagan	\$3,571,100	\$29,011,922	194,882	\$149
Columbia Shuswap-TO	0	435,934	35,739	12
Fraser Valley	0	500,000	7,096	70
North Okanagan	925,000	5,500,000	84,354	65
Okanagan Similkameen		4,385,674	83,022	53
Thompson Nicola		1,558,801	132,663	12
Columbia Shuswap-K			15,001	0
Kootenay Boundary		3,672,964	31,447	117
Central Kootenay		300,000	59,517	5
East Kootenay	845,000	3,496,600	60,439	58
Total	\$5,341,100	\$48,861,895	528,760	92

As the figures indicate, the cumulative impact of lending by SIDIT has been concentrated in the Central Okanagan, with approximately 60 percent of the loans funding deployed in the area. The next highest areas are North Okanagan and Okanagan Similkameen, with 11 and 9 percent respectively. This is a high percentage of loans being concentrated in a few regions. Although the current Strategic Plan goals support increased economic growth and diversity in the region, there does not appear to be a specific goal to increase the loan funds in areas that have not received much loan funding to date.

It is recommended that a strategy and implementation plan be created which specifically addresses the loan funding distribution by region.

Table 4 - Grant Funding by Region and Per Capita

Regions	2018	Cumulative	Population	\$ Per Capita
Central Okanagan	\$125,000	\$1,040,478	194,882	\$5
Columbia Shuswap-TO	\$25,000	\$250,000	35,739	\$7
Fraser Valley		\$25,000	7096	\$4
North Okanagan		\$348,022	84,354	\$4
Okanagan Similkameen	\$8,500	\$484,784	83,022	\$6
Thompson Nicola	\$100,000	\$1,249,666	132,663	\$9
Columbia Shuswap-K	\$3,000	\$178,000	15,001	\$12
Kootenay Boundary	\$112,000	\$1,018,726	31,447	\$32
Central Kootenay	\$75,000	\$686,088	59,517	\$12
East Kootenay	\$25,000	\$674,706	60,439	\$11
Total	\$473,500	\$5,955,470	528,760	\$11

The regional distribution of disbursed grants is less weighted to one particular region compared to the loans from Table 3.

It is recommended, in tandem with the loan distribution funding recommendation above, to create a strategy and implementation plan with an objective to create an even distribution of grants by region.

G. Marketing of SIDIT

In the past, SIDIT has presented to various business groups, Chambers, Rotary clubs, regional economic development officers, MLAs, other elected officials, chartered banks, credit unions, etc. to educate the audience about SIDIT.

A marketing strategy and plan is very important to SIDIT. Communicating the SIDIT message to stakeholders will inevitably lead to partnerships and opportunities. This plan will assist SIDIT in achieving **Goal 3** of the fiscal 2019–2021 Strategic Plan - Attract new capital to the Southern Interior region to drive incremental economic development activities, as well as **Goal 5** - Create and sustain public awareness of and support for the Trust's purpose, goals, achievements and successes with a focus on partnership development, collaboration and extending rural reach.

It is recommended, under the leadership of the CEO, that a renewed marketing strategy and companion plan be developed. It is recommended the marketing strategy and plan move beyond the region's borders. There are organizations in the lower mainland that could be a valuable partner for SIDIT.

H. New Policies

There were two policies missing that one would typically find in corporate policies.

It is recommended that whistle blower and business continuity policies be added to SIDIT's corporate policies.

I. Board Appointments

The government appoints five board members under the *Act*. For any organization, a full complement of Board members is very important. It is also important that the Regional Advisory Committees have a process of renewal and appointments of eight (8) Board members.

It is recommended the government appoint their board members promptly and that SIDIT support the Regional Advisory Committees in discharging their responsibilities.

Appendix 1

Documents reviewed:

Auditor General of British Columbia – Audit of Three Development Initiatives Trusts
Report April 2012

2018 – 2021 Strategic Plan

2006 – 2018 Annual Reports

Financial Management Policies – 3.07 Lending and Equity Investment Policy
(amended and approved March 22, 2018)

Lending and Portfolio Procedures and Guidelines – Updated March 22, 2018