



New Mexico
Small Business Investment Corporation

2017 Annual Report

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Alan Fowler, CMB
Board Chair and President
New Mexico Small Business
Investment Corporation



September 25, 2017

The Honorable Susana Martinez
Office of the Governor
490 Old Santa Fe Trail, Suite 400
Santa Fe, New Mexico 87501

Dear Governor Martinez:

On behalf of the members of the Board of Directors of the Small Business Investment Corporation, doing business as the New Mexico Small Business Investment Corporation ("NMSBIC"), I want to thank you for appointing us to this important organization and giving us the opportunity to serve our State.

The NMSBIC was formed in 2001 by the Small Business Investment Act, NMSA 58-29-1 et. seq., to create new job opportunities in communities statewide, and is funded by an allocation from the severance tax permanent fund pursuant to NMSA 7-27-5.15. Upon receipt of the independent audited financial statements, the NMSBIC Board of Directors is charged with reporting the organization's financial results to you in accordance with the provisions of the Act. The enclosed report is intended to serve that purpose. A copy of the report of the independent auditors for the NMSBIC's fiscal year ended June 30, 2017 is also enclosed.

The NMSBIC Board of Directors (the "Board") is comprised of all new members appointed by you beginning in mid-2011, and the State Treasurer who holds a permanent seat on the Board. The new Board members have reviewed and learned from the organization's investment history and implemented a strategy focused on expanding the NMSBIC's lending program. The enclosed report includes observations regarding past activities and actions taken by the Board to strengthen and grow the NMSBIC. Highlights of the report are as follows:

- Since inception, the NMSBIC has supported 11,300 jobs in New Mexico, with 4,174 loans to small businesses, in 216 communities throughout New Mexico.
- The NMSBIC engaged the Bureau of Business and Economic Research (BBER) to conduct an impact analysis, which was completed in 2017. The BBER report indicated that for every \$1 million in NMSBIC loans, 12 new jobs have been created, and 21 jobs have been saved.
- During the fiscal year \$2.2 million of net excess funds were returned by the NMSBIC to the severance tax permanent fund, based on net excess funds from the prior fiscal year. This was the primary reason for the decline in total assets to \$38.9 million as of June 30, 2017, from \$41.7 million the previous year.

- After new Board members were appointed by you in 2011, the organization changed its focus to expand its lending program. NMSBIC funds committed to the lending program have increased to \$23.4 million in 2017, from \$12.4 million in 2012; an increase to 62% of assets from 34% of assets. The focus on lending has resulted in a decline in equity investments. Funds committed to equity investments dropped to \$10.7 million in 2017, from \$17.5 million in 2012; a decrease to 28% of assets from 49% of assets.
- The change in net assets for the year was negative \$578,578, primarily due to losses on equity investments of \$874,012. Equity investments are likely to continue creating volatility in the NMSBIC's change in net assets through 2022.
- The NMSBIC changed its basis of accounting to the AICPA's Financial Reporting Framework for Small and Medium-Sized Entities, as more fully described in the Financial Highlights of the annual report, and the Notes to Financial Statements.
- Launa Waller, of Clovis, New Mexico, resigned from the NMSBIC board of directors in January 2017, resulting in one vacant position on the board.

On behalf of the members of the Board, I am pleased to report the changes we have made, and are making, to move the organization forward in a positive direction. We are committed to building a viable and sustainable structure to enable the NMSBIC to fulfill its mission of stimulating the state's economy and creating job opportunities throughout New Mexico, while preserving the NMSBIC's capital.

Respectfully submitted,

Alan Fowler, CMB
Board Chair and President



Alan Fowler, CMB
Board Chair and President
New Mexico Small Business
Investment Corporation



September 25, 2017

The Honorable Patricia A. Lundstrom, Chairwoman
New Mexico Legislative Finance Committee
325 Don Gaspar, Suite 101
Santa Fe, NM 87501

Dear Chairwoman Lundstrom:

On behalf of the members of the Board of Directors of the Small Business Investment Corporation, doing business as the New Mexico Small Business Investment Corporation ("NMSBIC"), I want to express our appreciation for having the opportunity to serve our State.

The NMSBIC was formed in 2001 by the Small Business Investment Act, NMSA 58-29-1 et. seq., to create new job opportunities in communities statewide, and is funded by an allocation from the severance tax permanent fund pursuant to NMSA 7-27-5.15. Upon receipt of the independent audited financial statements, the NMSBIC Board of Directors is charged with reporting the organization's financial results to you in accordance with the provisions of the Act. The enclosed report is intended to serve that purpose. A copy of the report of the independent auditors for the NMSBIC's fiscal year ended June 30, 2017 is also enclosed.

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Respectfully submitted,

Alan Fowler, CMB
Board Chair and President

Introduction

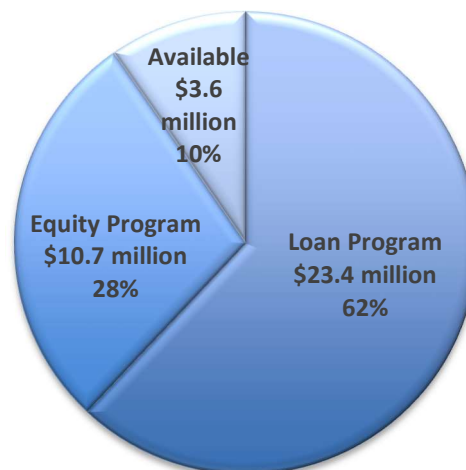
The Small Business Investment Corporation, doing business as the New Mexico Small Business Investment Corporation ("NMSBIC"), was formed by the Small Business Investment Act in 2001 to create new job opportunities in communities statewide, and is funded by an allocation from the severance tax permanent fund.

Investment Overview

The NMSBIC invests in New Mexico businesses through its lending and equity programs.

Governor Martinez appointed new board members to the NMSBIC in 2011. The new NMSBIC Board of Directors ("Board") changed the organization's strategy, to focus on expanding the NMSBIC's lending program. Reasons for expanding the NMSBIC's lending program were, (i) filling a lending gap due to a shortage of traditional bank lending available to small businesses in New Mexico, and (ii) the NMSBIC had experienced significant losses from its large concentration of equity program investments.

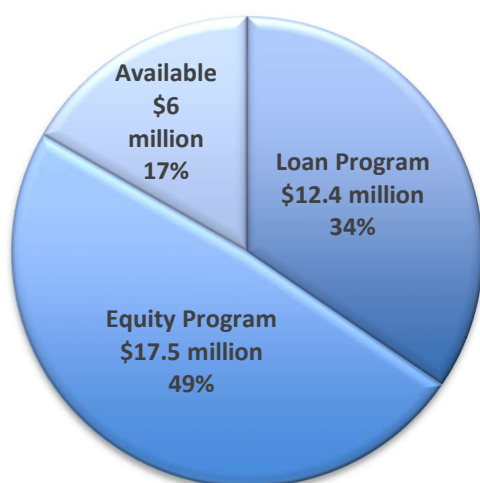
**Committed and Available Funds
June 30, 2017**



The above comparison shows the results of the NMBIC's strategy from 2012 to 2017:

- Lending program committed funds have increased to \$23.4 million from \$12.4 million; to 62% of assets from 34% of assets.
- Equity program committed funds have decreased to \$10.7 million from \$17.5 million; to 28% of assets from 49% of assets.

**Committed and Available Funds
June 30, 2012**



As of June 30, 2017, outstanding and committed balances for the lending and equity programs were as follows.

	Equity Program	Lending Program
Outstanding	\$ 10,426,049	\$ 18,546,211
Committed	\$ 264,551	\$ 4,828,789
Total	<u>\$ 10,690,600</u>	<u>\$ 23,375,000</u>

Impact

Through its lending program, NMSBIC is an important source of funding for New Mexico organizations engaged in micro-lending and small business lending in New Mexico. Lending partners include Accion, New Mexico Community Development Loan Fund (“The Loan Fund”), the New Mexico Mortgage Finance Authority (“MFA”), Rio Vista Growth Capital, and WESST Corp. Since its inception, and in connection with its lending partners, the NMSBIC has funded 4,174 loans to New Mexico start-up and small businesses that have supported an estimated 11,300 jobs throughout New Mexico.

4,174 loans
11,300 jobs

Since its inception in 2001, and in connection with its equity partners, the NMSBIC has committed \$33.3 million in equity investments to start or grow 48 New Mexico businesses. Equity partners have included Flywheel Ventures, Mesa Capital Partners, New Mexico Community Capital, New Mexico Mezzanine Partners, and Verge Fund. New Mexico businesses that are growing with equity funding from NMSBIC include, Aspen Avionics, BoomTime, IntelliCyt, Wellkeeper, and Miox. These are only a few of the active companies started with equity provided by NMSBIC.

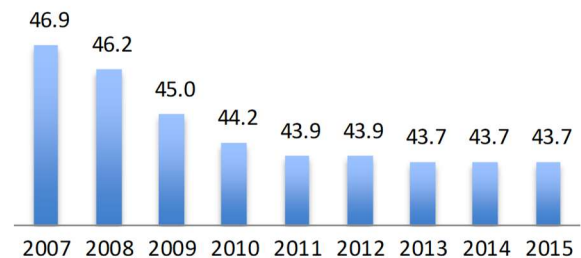
Equity Investments in 48 New Mexico Companies

The New Mexico Economy

New Mexico was impacted by the financial crisis that began in 2008. Employment and the number of business establishments declined, and the unemployment rate increased.

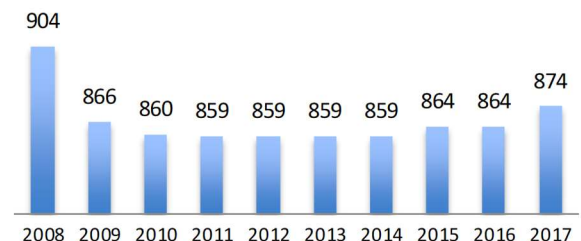
Recently released data for 2015 (most recent data available) from the Census Bureau’s County Business Patterns series show that the number of New Mexico business establishments has decreased since 2007.¹

**New Mexico Business Establishments
(in thousands)**



New Mexico employment increased in 2017 to 874,322, but has still not recovered to the June 2008 level of 904,430².

**New Mexico Employment
as of June 30 (in thousands)**

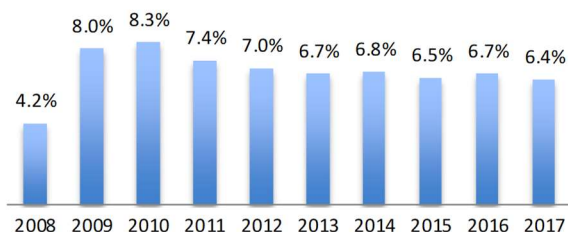


¹ Source: US Census Bureau, <https://factfinder.census.gov>

² Bureau of Labor Statistics, www.bls.gov

New Mexico's unemployment rate dropped from 6.7% at June 30, 2016, to 6.4% at June 30, 2017. The unemployment rate has declined from a high of 8.3% as of June 2010. However, unemployment has not returned to the June 2008 level of 4.2%³.

**New Mexico Unemployment Rate
as of June 30**



UNM's Bureau of Business and Economic Research provided the following forecast in their report, *FOR-UNM Bulletin, A Quarterly Forecast of the New Mexico Economy, Summer 2017*:

New Mexico Review and Outlook

According to the Bureau of Labor Statistics' QCEW employment data, New Mexico lost 2,500 jobs (-0.3%) the final quarter of 2016 (October-December), the first quarterly loss in five years. Suggesting a possible shift in the patterns of job growth, the poor performance in the fourth quarter was largely attributable to slowing employment growth in metro areas, from an average of 1.5% during the preceding four quarters to just 0.7% in the most recent quarter. Losses in non-metro areas of the state, while still deep (-1.9%), diminished slightly.

A similar shift is also evident in the industrial patterns of growth. Mining added jobs on a quarter-over-quarter basis for the first time since 2014, though the year-over-year numbers are still down sharply (-17.2%). By contrast, healthcare and social assistance, the principal driver of job growth for the past several years, showed signs of a slowdown (3,450 jobs, 3.0%, compared to an average of 4.4% over the preceding four quarters). Additionally, state

and local government jobs losses deepened (-1,450 jobs, -0.9%), reflecting the impact of two years of budget cuts.

BEA revised personal income data for 2016Q4, marking down growth from 2.3% to just 1.0%. Nearly all components were lowered. Total wage & salary disbursements were revised to -0.1%; private sector workers lost 0.2% in wages. According to newly released data, incomes rose by just 2.1% in 2017Q1, again weighed down by weak wage & salary growth (2.2%). Transfer payments increased by just 1.1%. After a nearly 75% increase since 2014, Medicaid payments declined by 3.7%, suggesting that the state has absorbed the full benefits of the Centennial Care program.

Real estate markets continue to gain ground. Statewide sales were up 7.7% and 10.6% in the first two quarters of 2017, and this is now generating a steady, if unspectacular, appreciation in values. However, increased sales and market values are yet to stir new residential construction; permitted construction was down 15% during the two-quarter period.

Although WTI oil prices slipped from a high of \$53.47/barrel in February to an average of \$45.18/barrel in July (since rebounded to \$50.19/barrel as of July 31), the number of drill rigs active in New Mexico continued to climb, from of 48 in February to an average 58.5 in June and July.

FOR-UNM forecasts employment growth of 0.8% for the remainder of 2017, pulling up the average for the year to 0.6%. The state will add 8,500 jobs (1.1%) in 2018 and an average of 10,000 (1.2%) during the next four years. In total, the state is forecast to add 54,000 jobs through 2022 (807,300 in 2016, 861,500 in 2022). This estimate is down from 59,000 in the April forecast.

On balance, stronger growth will be more the result of diminished losses in mining and related sectors than an acceleration of growth in the principal drivers. Employment losses in the mining sector will fade by end-2017. Employment will remain flat in 2018 and recover only very gradually thereafter (250 jobs, 1.2% per year). Government

³ Bureau of Labor Statistics, www.bls.gov

payrolls will take more time to stabilize, and net gains will be minimal thereafter.

The outlook for personal income is weaker than the April report. The change is due to the large revision to 2016 data and disappointing 2017Q1 data. The forecast calls for 2.5% growth of personal incomes in 2017, down from 3.2% in April; and 3.5% growth in 2018, down from 3.9%. Personal income growth will be held in check by slow growth and even declining Medicaid transfers; weak job growth and stagnant wages in the government sector; and a fading hope that a fiscal stimulus package will drive investment and proprietors' incomes higher.

The financial crisis that began in 2008 had an impact on several companies that received equity capital from NMSBIC and, at least in part, contributed to NMSBIC equity losses. While unemployment has improved since 2010, there is still a critical need for providing funds to protect existing jobs and promote job growth. NMSBIC believes the continued expansion of its lending program addresses a serious funding gap created by retrenchment in the banking community, and is the most effective way to deliver funding to New Mexico businesses in the current environment. Continued expansion of our lending program enables the NMSBIC to better preserve capital and to increase the turnover of that capital, thereby benefitting more small businesses in our state.

Observations

The NMSBIC Board of Directors ("Board") has reviewed and learned from the organization's investment history. The following are the Board's observations.

Concentrations

Beginning in 2001, the NMSBIC committed \$33.3 million to equity capital investments. While these

investments resulted in the establishment and growth of several New Mexico businesses, this was a high concentration of dollars in high-risk investment vehicles. When the financial crisis began in 2008, this high concentration of high-risk investments resulted in significant losses.

Equity Investments in New Mexico

NMSBIC's investment history has provided valuable experience and revealed significant challenges regarding venture capital investing as follows:

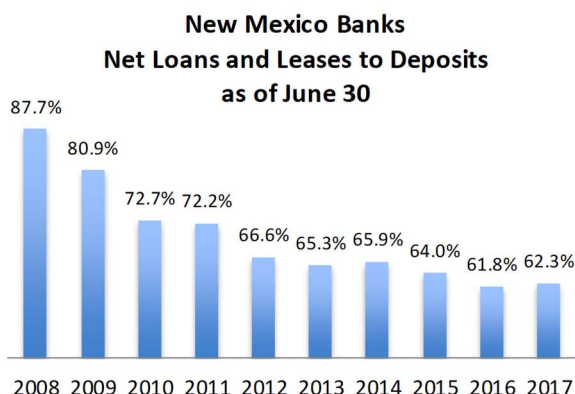
- NMSBIC's total asset size relative to the historical amount invested in each company resulted in limited diversification;
- NMSBIC only invests in New Mexico companies, which further limits diversification;
- High risk and limited diversification appears to have contributed to significant venture capital investment losses during the economic downturn;
- Management fees paid to equity fund managers has reduced investment returns;
- Equity investments are typically long-term, which reduces the ability to turnover capital in additional new small businesses;
- Equity investments do not provide current income to offset NMSBIC's operating expenses; and
- Equity investments have been geographically concentrated, with limited funding outside the Rio Grande Corridor.

Lending Gap

As a result of the financial crisis, there has been a tightening of bank lending to small businesses. As shown on the following page, the loan-to-deposit ratio for New Mexico-based banks improved from 61.8% at June 30, 2016, to 62.3% at June 30, 2017, but is still well below the June 2008 level of 87.7%.⁴ This tight credit market provides an opportunity for NMSBIC to expand its lending program and help fill

⁴ Source www.fdic.gov, Statistics on Depository Institutions

the current lending gap, especially for new and growing small businesses.



Actions and Changes

The NMSBIC has made the following changes and is taking action to strengthen the organization and capitalize on opportunities to stimulate economic growth in New Mexico.

Prudent Investor Rule

In 2011, the board adopted the Prudent Investor Rule as a basis for all future investments. The NMSBIC will continue to employ that rule in evaluating loan and investment opportunities. NMSBIC loans and investments shall be underwritten in a way that balances yield, safety, diversification, and economic development.

Expansion of Lending Program

The NMSBIC has been, and is continuing to expand its lending program. Advantages of the lending program include:

- Helping to fill a funding gap for small businesses in New Mexico;
- Smaller transaction size benefits more businesses;
- Shorter-term investments result in higher turnover of funds;
- No dilution from management fees;
- Current interest income offsets NMSBIC operating expenses;

- Borrower equity and collateral reduces risk of loss; and
- Funds are provided to communities throughout all of New Mexico.

Policies and Underwriting Criteria

The NMSBIC continues to evaluate lending partner policies and underwriting criteria to ensure proper controls are in place to mitigate loan loss risk related to an expansion of lending.

Lending Partner Agreements

The NMSBIC continues to review its agreements with lending partners to ensure that appropriate covenants are in place to protect both the NMSBIC and its lending partners, loan terms provide appropriate risk versus reward balance, and there is a reasonable expectation of a positive financial return and preservation of NMSBIC capital. During the fiscal year the NMSBIC made the following changes:

- The NMSBIC increased the maximum funding level for The Loan Fund's revolving line of credit from \$11 million to \$13 million. Under its loan agreement with The Loan Fund, the NMSBIC earns interest of 2.0% annually, and no loan losses are passed through to the NMSBIC.
- The NMSBIC increased the maximum funding level for ACCION's loan participation agreement from \$6.5 million to \$7.75 million, under new terms put in place in 2013. Under the new 2013 lending program with Accion, the NMSBIC earns interest of 3.0% annually, and the NMSBIC's loan losses are capped at 1.0% annually.

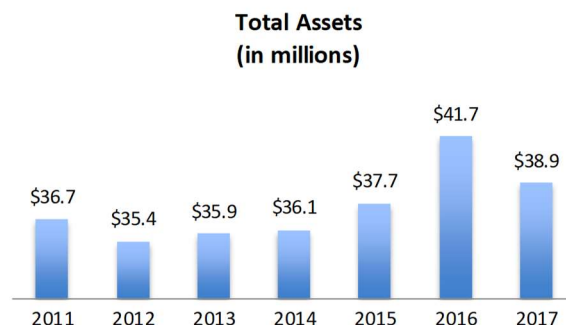
Financial Highlights

Attached to this report are NMSBIC's audited financial statements as of the fiscal years ended June 30, 2017 and 2016. Financial highlights are as follows:

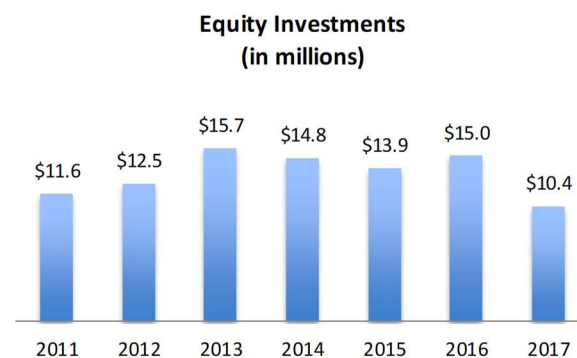
Change in Financial Accounting Framework

In 2017, it was determined the NMSBIC meets the definition of a governmental entity for purposes of accounting and financial reporting. NMSBIC's management and Board believe that standards promulgated by the Government Accounting Standards Board (GASB) are not appropriate for the NMSBIC, and that GASB-based financial statements would be less informative than financial statements based on the FASB framework.⁵ As a result, the NMSBIC changed its financial accounting framework to the Financial Reporting Framework for Small and Medium-Sized Entities (FRF for SMEs), developed by the American Institute of Certified Public Accountants (AICPA). Additional information is provided in Note 1 to the enclosed Financial Statements.

As of June 30, 2017, the NMSBIC ended its fiscal year with \$38.9 million in total assets, a decrease from \$41.7 million the previous year. The decrease was primarily due to, (i) a \$2.2 million payment of net excess funds to the severance tax permanent fund based on net excess funds from the prior fiscal year, and (ii) net realized and unrealized losses on equity investments of \$874,012.



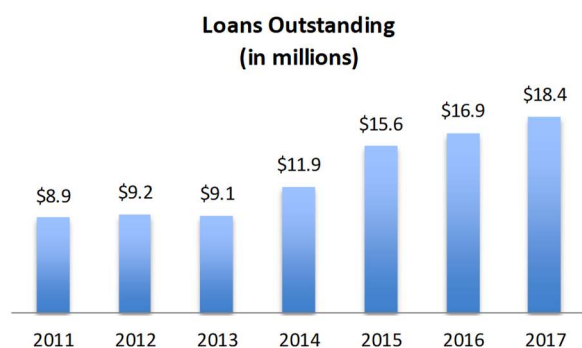
Equity investments decreased to \$10.4 million from \$15.0 million the previous year. Activity was comprised primarily of (i) \$3.7 million in net distributions received from equity funds, (ii) \$1.1 million in negative equity investment valuation adjustments, and (iii) equity investment realized gains of \$184,713.



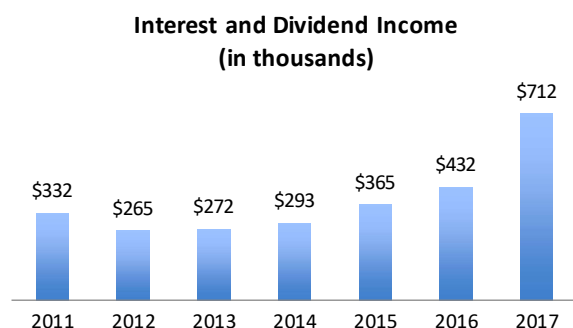
⁵ Statement No. 72 of the Governmental Accounting Standards Board, Paragraph B74 states, "... in connection with economic development activities, such as providing venture capital ... the ownership of common stock or another equity interest does not meet the definition of investment because the asset is held primarily to further the economic development objectives of the government program. In those

circumstances, the [GASB] Board concluded that the cost method is the appropriate measurement basis." NMSBIC's management and Board believe that using the cost method for equity investments would not be appropriate for the NMSBIC, and is an example of why management and the Board believe GASB-based financial statements would be less informative than financial statements based on the FASB framework.

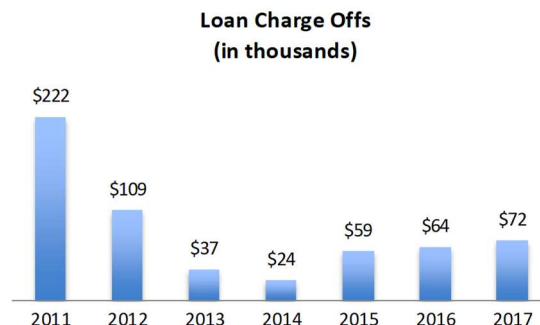
Loans, net of allowance for loan losses, increased to \$18.4 million from \$16.9 million the previous year. From 2011 to 2013, new loan demand was offset with loan payoffs, resulting in NMSBIC outstanding loan balances that were relatively flat. Since 2013, new loan demand has outpaced payoffs, resulting in net growth in outstanding loans.



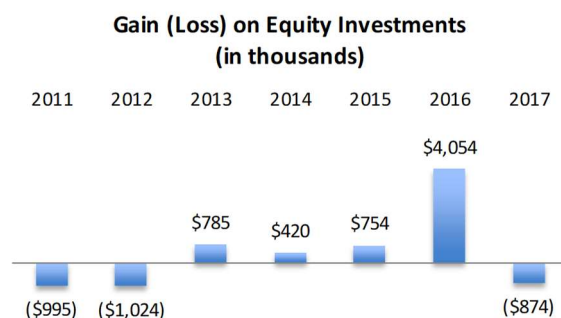
Interest and dividend income increased to \$711,570 in 2017, from \$431,950 the previous year, primarily due to (i) increases in outstanding loan balances and, and (ii) investment in a State Investment Council Core Plus US Bond Pool that generated a better return than previous investments in collateralized bank certificates of deposit.



Loan charge-offs have declined since 2011, in-part due to the NMSBIC's restructuring of its participation agreement with Accion, under which loan losses passed through to the NMSBIC are now limited to 1% of the outstanding loan balance. Loan charge-offs increased in 2017 to \$72,328, from \$64,256 the previous year. Loan charge-offs as a percentage of outstanding loans were unchanged in 2017 from 2016, at 0.4%.

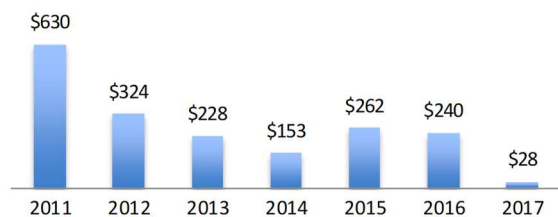


The \$4.1 million gain on equity investments in 2016 was primarily due to the sale of Intellicyt, which resulted in gains and distributions to the NMSBIC from both New Mexico Community Capital and the Verge Funds. In 2017 there was a net loss on equity investment of \$874,012, comprised of (i) negative equity investment valuation adjustments of \$1.1 million, and (ii) equity investment net realized gains of \$184,713. Approximately \$463,000 of the NMSBIC's loss on equity investments in 2017 was related to a company that was sold in 2014, and possible post-sale performance payments were not realized due to a down-turn in the oil and gas industry. The remaining losses were primarily negative investment valuation adjustments, spread over several different companies.



Management fees and expenses paid to equity funds, net of other income from equity funds, have declined primarily due to equity funds reaching the end of their fund lives, and declines in outstanding fund investments.

Equity Fund Management Fees, Operating Expense, and Other Income
(in thousands)

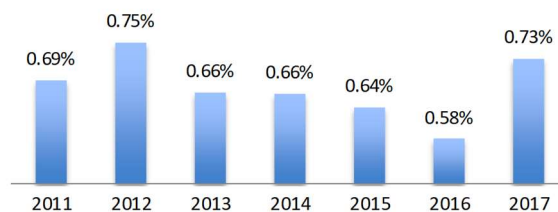


NMSBIC's direct operating expenses of \$282,465 in 2017, were higher than the previous year, and were comprised of \$118,973 in other program services, and \$163,492 in management and general expenses. With \$38.9 million in total assets, operating expenses were 0.73% of total assets in 2017. The increase in operating expenses in 2017 was primarily due to the NMSBIC's engagement of the Bureau of Business and Economic Research (BBER) to conduct an impact analysis.

NMSBIC Operating Expense
(in thousands)

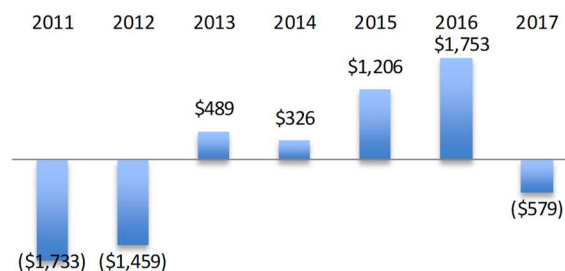


NMSBIC Operating Expense as a percent of Total Assets



The NMSBIC had a negative change in net assets in 2017 of \$578,578. Interest income of \$711,570 was offset by total expenses of \$374,283, and by net realized and unrealized losses on equity investment of \$874,012. Equity investments are likely to continue creating volatility in the NMSBIC's net income through 2022.

Net Income (Loss)
(in thousands)



NMSBIC Lending Partners



ACCION

WESST

Rio Vista Growth Capital

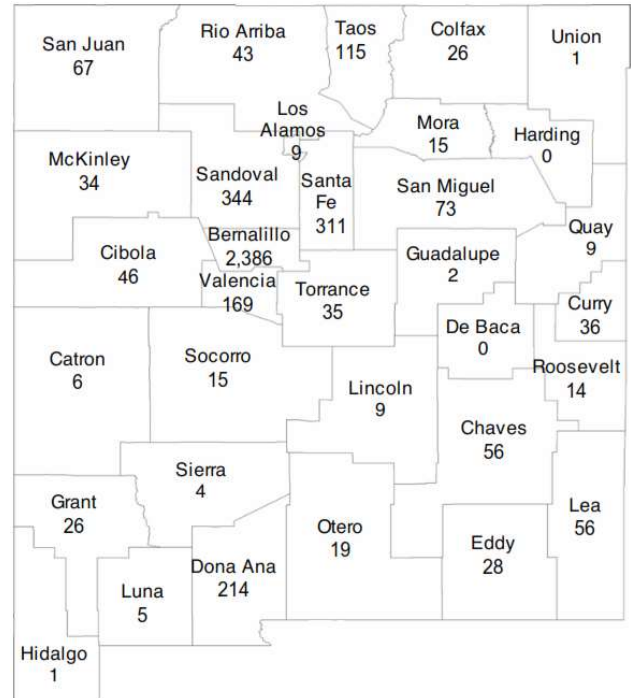
Lending Program

The NMSBIC's lending program provides funding to Accion, The Loan Fund, MFA, Rio Vista Growth Capital, and WESST.

Community Development Financial Institutions

Accion, The Loan Fund, and WESST, are designated as Community Development Financial Institutions (CDFIs) by the U.S. Department of the Treasury. CDFIs have a mission of providing financing in low-income communities and to people who lack access to financing.

The NMSBIC's lending partners have provided 4,174 loans to businesses in communities statewide, in many cases preserving jobs that would have been eliminated without access to capital. Through its lending program, the NMSBIC has provided over \$74 million in loans since 2001 to businesses that would likely not have had access to such loans from other sources. Loans typically range in size from \$2,500 to \$250,000 to small businesses throughout New Mexico. Loans have been made in 31 of 33 New Mexico counties.



Through its lending partners, the NMSBIC has provided funds for 4,174 loans in 31 of 33 counties in New Mexico.

Since inception, and through June 30, 2017, the NMSBIC has funded the following volume of loans through its lending partners:

	# of <u>Loans</u>	Jobs <u>Supported</u>	Loan <u>Volume</u>
The Loan Fund	596	3,613	\$36,820,152
Accion	3,522	7,306	\$33,706,798
MFA	4	112	\$2,300,000
RVGC	1	16	\$750,000
WESST	<u>51</u>	<u>253</u>	<u>\$599,878</u>
	4,174	11,300	\$74,176,828

As of June 30, 2017, the NMSBIC had the following amounts outstanding from, and committed to, its lending partners. Figures shown below for Accion are combined for the prior and new loan participation agreements.

	# of		
	<u>Loans</u>	<u>Outstanding</u>	<u>Committed</u>
The Loan Fund	140	\$9,373,903	\$13,000,000
Accion	526	\$7,517,796	\$7,750,000
MFA	1	\$800,000	\$1,500,000
RVGC	1	\$750,000	\$750,000
WESST	<u>11</u>	<u>\$104,512</u>	<u>\$375,000</u>
Totals	679	\$18,546,211	\$23,375,000

The above figures show over \$74 million in loans have been funded with \$23.4 million of committed funds. Over three times the committed capital has been loaned and recycled via repayments of interest and principal, providing tremendous leverage of the NMSBIC's capital. As noted above, loan losses to the NMSBIC were 0.4% of the outstanding balances. Given many of the borrowers would not qualify for traditional lending, the low loan losses under this program are impressive. The NMSBIC is working with its lending partners to continue expanding the lending program in a responsible manner.

NMSBIC Equity Partners



**New Mexico
Mezzanine
Partners**

Equity Program

Equity investments in New Mexico were virtually unheard of prior to 2000, but the efforts of the State Investment Council and the NMSBIC have attracted funds and investment professionals to New Mexico. Prior to 2004 there were no equity funds headquartered in New Mexico and no funds focused their capital and expertise exclusively on New Mexico companies. It was the NMSBIC's capital and early commitments that led to the investment in venture capital funds based in New Mexico.

Most large equity funds look to deploy \$5 to \$10 million in any one investment, whereas New Mexico had smaller, early stage companies that warranted investments of only \$250,000 to \$1 million. Few, if any, local companies would have been able to attract national attention and, without equity, could not have secured any credit relationships.

Beginning in 2004, the NMSBIC committed capital to Flywheel Ventures, Mesa Capital Partners, New Mexico Community Capital, New Mexico Mezzanine Partners, and Verge Fund to address the need for capital access for local start-ups, technology transfer licensees, and other small businesses looking to expand. With these five partners, NMSBIC has participated in eleven venture capital partnerships. Two of the partnerships that were managed by Mesa Capital Partners, and the Flywheel I-NMSBIC partnership, are now closed.

Cash invested (contributions made less distributions received) and current fair values as of June 30, 2017 are as follows:

(Dollars amounts in thousands \$000)

<u>Partner</u>	<u>Cash Invested</u>	<u>Current Value</u>
NM Gap Fund I	\$1,912	\$3,302
NM Comm. Capital	\$2,560	\$2,031
NM Mezzanine Ptrs	\$1,689	\$930
Verge I	\$368	\$516
Verge I.5	\$836	\$1,079
Verge II	\$246	\$1,418
Verge II.5	<u>\$844</u>	<u>\$1,150</u>
Totals	\$8,455	\$10,426

Capital committed to the above equity partners has been fully funded, with the exception of \$264,551 for Verge II.

Equity Program Activity

The following is a recap of equity fund activity during the past year:

- The Flywheel I-NMSBIC limited partnership reached its termination date as was closed. The value declined by \$200,616 during the year. The the investment resulted in a \$1.5 million loss over the life of the fund.
- For New Mexico Community Capital, the limited partners approved a one-year extension of the fund's termination date.
- For New Mexico Gap Fund I, the NMSBIC approved a one-year extension of the fund's termination date, with management fees of \$50,000, and up to \$16,000 in fund expenses.
- For New Mexico Mezzanine Partners (NMMP), the limited partners agreed to extend the fund to April 2018, with management fees of \$24,000, plus 1% of all payments received, which provided

the potential for an additional \$16,822 in management fees.

- For the Verge Funds, the limited partners approved one-year extensions for Verge I and Verge I.5, with annual management fees of \$30,000 and \$25,000, respectively. The limited partners also approved a business combination of two Verge II portfolio companies that resulted in a concentration in one company greater than 20% Verge II's total investments.

NMSBIC Impact

The following provides information regarding the impact of NMSBIC's lending and equity programs on New Mexico small businesses and jobs, and costs of delivering these services.

The Importance of Small Businesses

The NMSBIC's lending program supports small businesses in New Mexico. Small businesses are vitally important to both the New Mexico and national economies.

According to the Small Business Administration, a small business has 500 or fewer employees. In New Mexico, small business employment accounts for 56% of total employment. In 2014, there were 28,854 (87%) New Mexico small businesses with 1-20 employees, and 4,292 (13%) small businesses with 21-500 employees.⁶

According to the National Small Business Association, 73% of small firms used financing in the last 12 months. Small business financing needs vary greatly. For many firms, the lack of capital causes difficulties growing the business, financing future sales, and keeping adequate inventory.⁷

Nationally, small businesses comprise⁸:

- 99.9% of all firms
- 99.7% of firms with paid employees
- 97.6% of exporting firms (287,835 small exporters)
- 32.9% of known export value (\$440 billion out of \$1.3 trillion)
- 47.8% of private sector employees (58 million out of 121 million employees)
- 41.1% of private-sector payroll

Nationally, small businesses accounted for 61.8% of net new jobs from the first quarter of 1993 until the third quarter of 2016.⁹

⁶ *New Mexico Small Business Profile 2017*, U.S. Small Business Administration Office of Advocacy

⁷ *Frequently Asked Questions About Small Business Finance*, July 2016, U.S. Small Business Administration Office of Advocacy

Jobs Supported

A common measure used by CDFI's and by the Small Business Administration (SBA) is total jobs at the time a loan is originated, referred to as "jobs supported." In the table on page 16, *Equity and Lending Programs, Jobs Supported and Cost per Job*, information is provided regarding New Mexico jobs supported by the NMSBIC's equity and lending programs. For the equity program, jobs supported are the number of jobs as of June 30, 2017, or as of the date when the company exited from the NMSBIC's investment portfolio. For the lending program, jobs supported are the total jobs when the loan was originated. Jobs supported are self-reported by the NMSBIC's equity and lending partners.

- The equity program has had a life-to-date loss of \$10.0 million, with 412 jobs reported at June 30, 2017, resulting in an estimated cost per job supported of \$24,359. Equity investments are long-term in nature, therefore year-to-date results are not considered meaningful.
- The lending program has had life-to-date net interest income, after loan losses, of \$1,722,505, with 11,300 jobs reported, for an estimated *profit* per job supported of \$152. For the twelve months ended June 30, 2017, net interest income was \$377,829, with 1,075 jobs reported, for an estimated *profit* per job supported of \$351.

⁸ *Frequently Asked Questions About Small Business*, August 2017, U.S. Small Business Administration Office of Advocacy

⁹ *Frequently Asked Questions About Small Business*, August 2017, U.S. Small Business Administration Office of Advocacy

BBER Impact Analysis

The NMSBIC engaged the Bureau of Business and Economic Research (BBER) to conduct an impact analysis. There were four proposed phases, of which the first phase was completed in 2017. The number of jobs were independently measured by BBER. The BBER analysis indicated the NMSBIC's equity and lending programs resulted in the creation of 646 "new" jobs in New Mexico during the five-year period from July 1, 2010 to June 30, 2015. Additionally, the BBER study estimated 750 New Mexico jobs were saved.

The BBER analysis included a supplement that calculated the cost per new job, based on an "opportunity cost" of funds using the severance tax permanent fund's (STPF) target return of 6.75%. The BBER analysis reported an equity program cost per new job of \$29,085, and a lending program cost per new job of \$4,717.

The lending program cost per new job of \$4,717 compares favorably with cost per job figures (also five-year averages) for the state's Job Training Incentive Program (JTIP) and Local Economic Development Act (LEDA) program, of \$5,941 and \$4,255, respectively, as noted in the BBER impact analysis.

As shown in the table on page 16, *Equity and Lending Programs, Jobs Supported and Cost per Job*, the NMSBIC's lending program is profitable, self-sustaining, and operates with positive net cash flow. The BBER analysis applied a more rigorous method, using a theoretical opportunity cost of funds based on the STPF target return. BBER's more rigorous method of applying an opportunity cost resulted in the \$4,717 cost per new job figure stated above.

The NMSBIC's lending program is profitable, self-sustaining, and operates with positive net cash flow

The BBER analysis also indicated that during the five-year period, the cumulative impact of the NMSBIC's programs over a five-year period was the direct and indirect support of \$23.9 million of labor income, and \$69 million in economic output in New Mexico.

A study was conducted in August 2013 by the US Census Bureau and the Institute for the Study of Labor, on new jobs created by the Small Business Administration (SBA)¹⁰. The study noted that SBA has historically reported a performance indicator which is the number of "jobs supported" by its lending program. The purpose of the study was to measure the number of "new" jobs created by the SBA's lending program. The study found that 5.4 new jobs were created for each \$1 million loaned by the SBA, from 1976 to 2010.

Based on the recent BBER impact analysis performed for the NMSBIC, \$35.6 million of NMSBIC loans were originated from 2011 to 2015 resulting in 426 new jobs (lending program only), or 12.0 new jobs for each \$1 million in loans, which appears to compare favorably to the SBA's ratio of 5.4 new jobs for each \$1 million in loans. In addition, the BBER study indicated the NMSBIC's lending program saved 750 jobs from being lost, or 21 jobs for every \$1 million in NMSBIC loans originated.

For every \$1 million in new NMSBIC loans, the impact has been 12 new jobs, and 21 existing jobs saved

If we apply these results to \$74.2 million in NMSBIC loans originated since inception, it would indicate

¹⁰ *Do SBA Loans Create Jobs?*, J. David Brown and John S. Earle, August 2013

the NMSBIC's lending program has created 890 new jobs, and has saved 1,558 existing jobs in New Mexico.

The BBER analysis supports the NMSBIC board's strategy to focus on expanding our lending program. The full BBER report is available at www.nmsbic.org.

Impact on New Mexico Small Businesses

As noted above, the BBER impact analysis estimated that during a five-year period, 750 jobs would have been lost, if not for the NMSBIC's lending program. The following are excerpts from interviews with small business owners in New Mexico, regarding the impact of funding provided by the NMSBIC's lending program partners, as published by www.financenewmexico.org:

"The Loan Fund has been a lifesaver ... They kept me afloat."

- Christina Montoya of Montoya Bus Company. Montoya continues to work with The Loan Fund to finance new buses as needed. Today her company is the largest bus company in the Silver City/Bayard area, with 16 full-time, and 5 part-time employees.

*"If it wasn't for **Accion**, we wouldn't be here."*

- Mauro Nava of Clínica la Esperanza, a health clinic that serves Albuquerque's South Valley.

"We went to a lot of banks for financing, but [other lenders] didn't have a lot of appetite for startups. Most didn't even look at our numbers."

- Daniel Romero and Lori Griego worked hard to get the right ingredients to finance their Frost Gelato Shoppe, with help from **The Loan Fund**.

*"It wasn't a big loan, maybe \$20,000. But it enabled me to get over the hump ... **Accion** is critical, because the (business) failure rate for zero to five years — especially for restaurants — is ginormous."*

- Nico Ortiz, owner of Turtle Mountain Brewing in Rio Rancho. Accion helped to sustain his business until its fifth birthday, when traditional lenders were willing to lend. Today the company employs nearly three times as many people as it did in 1999, and its gross revenue has quadrupled.

"We could not have grown as aggressively as we did during a recession if we didn't have financing to support it."

- Peter Sanchez, Atrisco Heritage Foundation, speaking about his relationship with **The Loan Fund**.

*"I would not be able to bid on these extra projects if I didn't have [the loan from **Accion**] ... They're really a key component of my growth."*

- Gary Peterson, One Community Auto, speaking about the Accion loan that enabled him to bid on government contracts. Peterson's company purchases old vehicles that are used to train firefighters how to extract accident victims in emergency situations.

"A traditional lender wasn't interested in lending to a startup with no experience in the industry; at the time, breweries were lumped into the 'restaurant' (category) — a much riskier segment to finance."

- Gabe Jensen, co-owner of Bosque Brewing speaking about his **Accion** \$100,000 loan.

“(Accion) gave me the leg-up I needed ... It will help my business grow in ways it (otherwise) couldn’t have.”

- Cathy Schueler, executive director of Bosque Mental Health, a business that employs 14 people and provides a vital, and often life-changing, service to Individuals and Families across Albuquerque.

*“Our partnership with and support by **The Loan Fund** has meant the growth of our business ... Without (it), we would not have been able to grow, provide a greater array of services, keep pace with technological developments in our industry and hire additional people. The Loan Fund is more flexible about what constitutes collateral, and it understands the hurdles faced by rural or high-tech or unusual businesses.”*

- Tami Wiggins CEO Blue Skies Consulting, on her relationship with The Loan Fund

“If I hadn’t gotten the loan, I wouldn’t be here ... It’s paying itself off quite nicely.”

- Lyndseyanne Wilken, Run as One Tack and Equine. A loan officer at an area bank referred Wilken to **Accion**, thinking the nonprofit lender would be a good fit for her home-based venture. Even if the bank had been able to finance a startup like Run as One, it would have had to classify her loan as a machine loan, Wilken said, and the minimum for that loan type is \$10,000. Wilken obtained a \$5,000 loan from Accion to cover the costs of a leather sewing machine and other essential startup materials.

“The trust they have had in us is something for which we will always be grateful.”

- Julianna Garcia, co-owner of Pet Planet, a client of **The Loan Fund**.

Equity and Lending Programs, Jobs Supported and Cost per Job

Equity Program Costs and Benefits, Life-to-Date, June 30, 2017 (1):

	Net	Estimated		Jobs	Estimated
	Investment	Value	Gain (Loss)	Supported (2)	Profit (Cost)
					per Job
1 Santa Fe Windows and Doors (3)	(\$25,000)	\$0	\$25,000	n/a	n/a
2 Flywheel Ventures (2 funds)	\$3,411,989	\$3,302,233	(\$109,756)	74	(\$1,483)
3 NM Community Capital	\$2,599,692	\$2,030,957	(\$568,735)	219	(\$2,597)
4 Mesa NM Growth Funds (2 Funds)	\$10,257,750	\$0	(\$10,257,750)	18	(\$569,875)
5 NM Mezzanine Ptrs	\$1,688,976	\$930,203	(\$758,773)	41	(\$18,507)
6 Verge Funds (4 funds)	\$2,528,345	\$4,162,656	\$1,634,311	128	\$12,768
7 Adjustment for multiple funds invested in the same company (4 companies)				-68	
8 Total Equity Program	\$20,461,752	\$10,426,049	(\$10,035,703)	412	(\$24,359)

9

10 (1) Equity fund investments are long-term investments. Life-to-date results are considered more meaningful
11 than year-to-date information.

12 (2) Jobs reported at June 30, 2017, plus jobs reported as of the date when a company was sold.

13 (3) Santa Fe Windows and Doors was originated in 2003 and repaid in full in 2007. This was the only direct investment
14 made by the NMSBIC.

15

Lending Program Costs and Benefits:

	Interest	Loan Charge	Net Interest	Jobs	Profit (Cost)
	Income	Offs	Income (Loss)	Supported (6)	per Jobs
					Reported
18 <u>Since Inception</u>					
19 ACCION 2003 Participation Agreement (4)	\$1,004,270	(\$1,293,305)	(\$289,035)	5,201	(\$56)
20 ACCION 2013 Participation Agreement	\$410,871	(\$132,108)	\$278,763	2,105	\$132
21 New Mexico Mortgage Finance Authority	\$37,186	\$0	\$37,186	112	\$332
22 THE LOAN FUND Participation Agreement (5)	\$77,631	(\$11,518)	\$66,113	-	-
23 THE LOAN FUND Line of Credit	\$1,506,581	\$0	\$1,506,581	3,639	\$414
24 Rio Vista Growth Capital Line of Credit	\$114,387	\$0	\$114,387	16	\$7,149
25 WESST Participation Program	\$26,205	(\$17,695)	\$8,510	253	\$34
26 Total Lending Program	\$3,177,131	(\$1,454,626)	\$1,722,505	11,300	\$152

27

12 months ended June 30, 2017

29 ACCION 2003 Participation Agreement (4)	\$13,257	(\$10,837)	\$2,420	-	-
30 ACCION 2013 Participation Agreement	\$184,473	(\$61,491)	\$122,982	685	\$180
31 New Mexico Mortgage Finance Authority	\$18,561	\$0	\$18,561	-	-
32 THE LOAN FUND Line of Credit	\$187,248	\$0	\$187,248	386	\$485
33 Rio Vista Growth Capital Line of Credit	\$44,399	\$0	\$44,399	-	-
34 WESST Participation Program	\$2,219	\$0	\$2,219	4	\$555
35 Total Lending Program	\$450,157	(\$72,328)	\$377,829	1,075	\$351

36

37 (4) The ACCION 2003 participation agreement was terminated as of November 1, 2013. Loans outstanding as of the
38 termination date will run off in the normal course of business.

39 (5) THE LOAN FUND 2004 participation agreement was terminated as of July 13, 2007.

40 (6) Jobs reported at the time the loan was originated.

Financial Education

The NMSBIC is committed to promoting financial education and financial literacy throughout New Mexico. NMSBIC's financial education efforts are highlighted below.

Finance New Mexico

The NMSBIC helped to create and continues to support a statewide business financial literacy resource called Finance New Mexico (www.financeenewmexico.org). The organization was selected in 2009 as the Albuquerque Chamber of Commerce Small Business Advocate of the Year. Each week, business-related articles are published in several New Mexico newspapers and also circulated electronically to businesses and economic development organizations throughout the state. In 2013, Finance New Mexico introduced its "Grow It!" program in partnership with the New Mexico Municipal League. When a business registers in their local community, a Grow It! package is delivered to the business with information about financial resources and services available to small businesses in New Mexico. Finance New Mexico plays an important role in publicizing the NMSBIC's programs in all corners of the State.

Albuquerque Community Meeting: Accessing Capital in New Mexico

In October 2016, the NMSBIC presented a community meeting in Albuquerque entitled, *Accessing Capital in New Mexico*. The meeting included presentations from representatives of the, the Small Business Development Center, The Loan Fund, Accion, WESST, Verge Fund, Flywheel Ventures, and the NMSBIC. This meeting continued the tradition of holding community outreach meetings throughout the state. In prior years the Board has held community outreach meetings in Los Lunas, Clovis, Española, Hobbs, Taos, Farmington, Las Cruces, and Santa Fe. It is the Board's intention to continue to hold a community meeting in areas around New Mexico each year.

Board Engagement

NMSBIC Board members have actively engaged in various activities to support the organization. Board members have attended numerous community events, attended meetings with existing and potential equity and lending partners, and performed detailed loan and operational reviews at lending partner offices. The NMSBIC Board members are qualified professionals who are applying their collective and diverse business experience in reviewing activities and making sound decisions. The Board members have demonstrated their dedication and commitment to strengthening and improving the NMSBIC.

Board Strategic Plan

The NMSBIC's strategic plan is focused on key initiatives to:

- Continue to focus on expanding the lending program throughout the entire state of New Mexico with existing and potential new partners; and
- Maintain the NMSBIC's self-sufficiency through lending program growth, so that interest income from loans and other interest earning assets exceeds operational expenses.

Statutory Requirements

The following information is provided in accordance with NMSA 58-29-6(B) and 58-29-7.

Audited Financial Statements

NMSBIC independently audited financial statements for the years ended June 30, 2017 and 2016 are attached to this report.

Rate of Return

For the fiscal year ended June 30, 2017, the NMSBIC had a negative change in net assets of \$578,578, which was a negative 1.48% return on the net assets of \$39,033,516 million from the beginning of the fiscal year.

Desired Changes in the Corporation

The NMSBIC Board recommends NMSA 58-29-7 be repealed, thereby removing the requirement that “net excess funds” be returned to the severance tax permanent fund. The effect of this change would be to help the NMSBIC self-fund the future expansion of its lending program, which is providing much needed capital to small businesses, and protecting and supporting jobs throughout New Mexico.

Also, Launa Waller, of Clovis New Mexico, resigned from the NMSBIC Board in January, 2017. This vacant Board position is appointed by the Governor, and is available to be filled, should the Governor choose to do so.

Continued Operation of the Corporation

The NMSBIC Board recommends continued operation of the corporation with a focus on expanding its lending program to address a gap in available bank financing as described in this report.

Severance Tax Fund Distribution

Under NMSA 58-29-7, the NMSBIC is charged with making a distribution of “net excess funds” to the severance tax permanent fund, calculated as return on investments to the corporation in the amount of dividends and interest actually received, plus any capital gains actually realized, less the operating expenses of the corporation and less amounts reasonably reserved for losses. For the fiscal year ended June 30, 2017, this calculation resulted in a negative number (see detail below) resulting in no distribution to the severance tax permanent fund.

Interest and dividends received, cash basis	\$ 686,567
Operating expenses, net of loan losses	(310,804)
Accumulated reserve for debt and equity losses	(1,496,422)
Capital gains realized	184,713
Net excess funds	<u>\$ (935,946)</u>

Conclusion

The NMSBIC is grateful for the support of the Governor, State Legislators, the State Investment Council, and its financial partners. Through the creation and expansion of the NMSBIC, New Mexico has created a unique delivery system of loans and investment capital for new and growing businesses.

Lending partners have provided 4,174 loans to businesses in communities statewide, in many cases preserving jobs that would have been eliminated without access to capital, and creating jobs that would not exist without NMSBIC funds. Through its lending program, the NMSBIC has provided over \$74 million in loans to businesses that would likely not have had access to capital. Additionally, a recent BBER study indicated that for every \$1 million in new NMSBIC loans, the impact has been 12 new jobs, and 21 existing jobs saved.

While equity program losses since the NMSBIC's inception have been substantial, there are several new companies that are growing and prospering with equity provided by NMSBIC. The impact NMSBIC has had in helping to create an equity/venture community has been positive, but the role the NMSBIC has been asked to play in this arena was, in some instances, ill-conceived. The NMSBIC Board plans to continue to decrease the investment concentration in these high-risk investments.

With the reduction in traditional lending activity and heightened regulatory constraints imposed on banks, access to loans continues to be challenging for New Mexico small businesses. The NMSBIC, through its lending partners, plays an important role in helping to fill that void. This program, created by the legislature, has been and continues to be a valuable State resource in investing taxpayer dollars in New Mexico businesses, in creating jobs for New Mexicans, and in having a positive impact on our State's economic health.

Going forward, the NMSBIC plans to continue reducing the concentration of equity investments, and to continue increasing the level of its lending activities to achieve a more balanced level of risk for the organization, while delivering much needed funding for loans to New Mexico businesses.

Respectfully submitted,

Alan Fowler, CMB
Board Chair & President

NMSBIC Board of Directors

Alan Fowler, CMB
NMSBIC Board Chair and President
Executive Vice President, First Mortgage Company
Albuquerque, New Mexico

Steven Morgan
NMSBIC Secretary/Treasurer
President, Bosque Consulting Group
Conchas Dam, New Mexico

The Honorable Tim Eichenberg, State Treasurer
State of New Mexico Office of the Treasurer
Santa Fe, New Mexico

Joseph Badal
NMSBIC Vice Chair and Vice President
President and CEO, Joseph Badal & Associates
Sandia Park, New Mexico

Roxanna Meyers
NMSBIC Past Board Chair
President/Owner, Century Sign Builders
Albuquerque, New Mexico

Lupe Garcia
Owner, Garcia's Tires
Santa Cruz, New Mexico

NMSBIC Executive Director/Investment Advisor

Russell Cummins
Owner, RDC Advisors LLC
Tijeras, New Mexico



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EXHIBIT A

Independently Audited Financial Statements
as of and for the years ended
June 30, 2017 and 2016

Small Business Investment Corporation

FINANCIAL STATEMENTS

June 30, 2017 and 2016

INDEPENDENT AUDITORS' REPORT

Board of Directors
Small Business Investment Corporation

We have audited the accompanying financial statements of Small Business Investment Corporation, also known as the New Mexico Small Business Investment Corporation (NMSBIC), which comprise the statements of financial position – American Institute of Certified Public Accountants (AICPA) Financial Reporting Framework for Small and Medium-sized Entities (AICPA FRF for SMEs) as of June 30, 2017 and 2016, and the related statements of activities and changes in net assets – AICPA FRF for SMEs, and cash flows – AICPA FRF for SMEs, for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the FRF for SMEs issued by the (AICPA FRF for SMEs), as described in Note 1; this includes determining that the basis of accounting is an acceptable basis for the preparation of financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to NMSBIC's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of NMSBIC's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of NMSBIC as of June 30, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with the FRF for SMEs, as described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared in accordance with the FRF for SMEs issued by the AICPA, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

Emphasis-of-Matter Regarding Investments

As discussed in Note 1 and Note 7, these financial statements include investments in partnerships valued by the general partner of each partnership in the absence of readily ascertainable market values. At June 30, 2017 and 2016, that portion of NMSBIC's investments was \$10,426,049 and \$14,994,617, respectively, which represents 27% and 38% of NMSBIC's net assets at those dates. Because of the inherent uncertainty of valuation of these investments, the estimate by each general partner of these values may differ significantly from values that would have been used had a ready market for those investments existed, and the difference could be material. Our opinion is not modified with respect to this matter.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The schedules of activity of debt cooperative agreements and the schedules of activity of equity cooperative agreements on pages 17 and 18 are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

September 25, 2017


Pulakos CPAs, PC

Small Business Investment Corporation

STATEMENTS OF FINANCIAL POSITION

June 30, 2017 and 2016

<u>Assets</u>	<u>2017</u>	<u>2016</u>
Current assets		
Cash and cash equivalents	\$ 1,331,817	\$ 3,168,048
Investment held with NM State Investment Council	8,262,462	3,051,478
Equity fund receivable	413,078	3,536,230
Prepaid expenses	4,239	4,239
Total current assets	10,011,596	9,759,995
Deferred interest receivable	54,346	32,446
Equity investments in New Mexico entities	10,426,049	14,994,617
Cooperative loan agreements, net of allowance for losses	18,378,674	16,876,599
	<u>\$ 38,870,665</u>	<u>\$ 41,663,657</u>
 <u>Liabilities and Net Assets</u>		
Current liabilities		
Accounts payable	\$ -	\$ 4,000
Debt funding payable, net	415,727	434,580
Due to severance tax permanent fund	-	2,191,561
Total current liabilities	415,727	2,630,141
Temporarily restricted net assets	38,454,938	39,033,516
	<u>\$ 38,870,665</u>	<u>\$ 41,663,657</u>

Small Business Investment Corporation

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

Years Ended June 30, 2017 and 2016

	2017			2016		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
Revenues and other support:						
Interest and dividend income	\$ -	\$ 711,570	\$ 711,570	\$ -	\$ 431,950	\$ 431,950
Realized gains on investments	-	184,713	184,713	-	3,706,916	3,706,916
Investment valuation adjustments	-	(1,100,578)	(1,100,578)	-	391,782	391,782
Net assets released from restrictions	374,283	(374,283)	-	2,778,134	(2,778,134)	-
Total revenues and other support	374,283	(578,578)	(204,295)	2,778,134	1,752,514	4,530,648
Expenses:						
Program services						
Equity investment operating expense, net	28,336	-	28,336	240,340	-	240,340
Provision for loan losses	63,482	-	63,482	18,612	-	18,612
Other program services	118,973	-	118,973	202,333	-	202,333
Net excess funds expense	-	-	-	2,191,561	-	2,191,561
Total program services	210,791	-	210,791	2,652,846	-	2,652,846
Management and general	163,492	-	163,492	125,288	-	125,288
Total expenses	374,283	-	374,283	2,778,134	-	2,778,134
Change in net assets	-	(578,578)	(578,578)	-	1,752,514	1,752,514
Net assets at beginning of year	-	39,033,516	39,033,516	-	37,281,002	37,281,002
Net assets at end of year	\$ -	\$ 38,454,938	\$ 38,454,938	\$ -	\$ 39,033,516	\$ 39,033,516

See Notes to Financial Statements and Independent Auditors' Report.

Small Business Investment Corporation

STATEMENTS OF CASH FLOWS

Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Change in net assets	\$ (578,578)	\$ 1,752,514
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities		
Change in provision for loan losses	63,482	18,612
Net loss (gain) on investments and investment fees	944,202	(3,864,861)
Changes in operating assets and liabilities		
Interest and dividends receivable	-	201
Equity fund receivable	3,123,152	(3,340,843)
Prepaid expenses	-	(19)
Deferred interest receivable	(21,900)	(19,925)
Accounts payable	(4,000)	4,000
Debt funding payable	(18,853)	63,233
Due to severance tax permanent fund	(2,191,561)	2,191,561
	<u>1,315,944</u>	<u>(3,195,527)</u>
Cash provided (used) by operating activities		
Cash flows from investing activities:		
Maturity of certificates-of-deposit	-	1,000,000
Purchase of investment held with NM State Investment Council	(5,252,837)	(3,000,000)
Investments in New Mexico entities	2,100,662	1,433,487
	<u>(3,152,175)</u>	<u>(566,513)</u>
Cash used by investing activities		
Change in cash and cash equivalents	(1,836,231)	(3,762,040)
Cash and cash equivalents, beginning of year	<u>3,168,048</u>	<u>6,930,088</u>
Cash and cash equivalents, end of year	<u>\$ 1,331,817</u>	<u>\$ 3,168,048</u>

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The Small Business Investment Corporation, also known as the New Mexico Small Business Investment Corporation (NMSBIC), is a nonprofit, independent, public corporation established by the New Mexico Small Business Investment Act, §58-29-1 et. Seq., NMSA1978, as amended (the Act). NMSBIC was formed to create new job opportunities by making equity investments in land, buildings or infrastructure for facilities to support new or expanding businesses in the State of New Mexico and to otherwise make debt investments and equity investments to create new job opportunities to support new or expanding businesses. NMSBIC's sole funding source is the New Mexico severance tax permanent fund.

NMSBIC seeks to establish programmatic, contractual relationships with existing and newly created providers of financial services to efficiently and effectively deliver capital for the purpose of creating new job opportunities and economic growth in the State of New Mexico. NMSBIC accomplishes this by providing capital for equity investments or loans for land, buildings or infrastructure to support new or expanded businesses, or equity investments or loans to New Mexico small businesses, to help support economic growth and job creation, and to otherwise enhance economic development objectives of the State of New Mexico.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual events and results could differ from those assumptions and estimates. The most significant estimates involve the fair value of debt and equity securities. Because of inherent uncertainty in valuing these investments, the estimated fair value may differ from the values that would have been used had a ready market for the investments existed.

Income Taxes

NMSBIC is a nonprofit charitable corporation and has been recognized as tax-exempt under Section 501(c)(4) of the Internal Revenue Code. NMSBIC has adopted accounting principles generally accepted in the United States of America as they relate to uncertain tax positions, and has evaluated its tax positions taken for open tax years. Currently, the 2014, 2015 and 2016 tax years are open and subject to examination by the Internal Revenue Service and New Mexico Taxation and Revenue Department. Management believes that the activities of NMSBIC are within their tax-exempt purpose, and that there are no uncertain tax positions.

Financial Instruments

The carrying amounts of cash and cash equivalents, receivables, payables, and other liabilities approximate fair value due to the short maturity periods of these instruments.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Financial Reporting Framework

A financial reporting framework is a set of criteria used to determine measurement, recognition, presentation, and disclosure of all material items appearing in the financial statements. The choice of a financial reporting framework rests with the owners and managers of an entity, in consideration of their needs and the needs of the users of their financial information. Certain frameworks constitute accounting principles generally accepted in the United States of America (GAAP), while others are non-GAAP ‘special purpose’ frameworks. Because its Board of Directors is appointed by the Governor of the State of New Mexico, NMSBIC is considered to be a governmental entity under GAAP.

The accompanying financial statements have been prepared using the Financial Reporting Framework for Small and Medium-Sized Businesses (FRF for SMEs), a special purpose framework developed by the American Institute of Certified Public Accountants (AICPA). The FRF for SMEs reporting option is intended for management, owners, and others who require financial statements that are prepared in a consistent and reliable manner in accordance with a non-GAAP framework that has undergone public comment and professional scrutiny. The accounting principles comprising it are appropriate for small and medium-sized entities, based on the needs of the financial statement users and cost and benefit considerations.

As described in the ‘Change in Financial Reporting Framework’ section following, NMSBIC selected the FRF for SME’s because, as a business entity, the information provided by the governmental framework is not best suited to the needs of the users of NMSBIC’s financial statements.

Change in Financial Reporting Framework

In previous years, NMSBIC presented financial statements using accounting principles promulgated by the Financial Accounting Standards Board (FASB), which were considered by NMSBIC’s management, its Board of Directors and its auditors to constitute GAAP. In 2017, it was determined that NMSBIC meets the definition of a governmental entity for purposes of accounting and financial reporting because its Board of Directors is appointed by the Governor of the State of New Mexico. GAAP for governmental entities is specified by standards promulgated by the Governmental Accounting Standards Board (GASB). Because GASB standards differ substantially from those of the FASB, adopting the GASB framework would entail changes in NMSBIC’s accounting and financial reporting.

Management and the Board of Directors of NMSBIC believe that the GASB framework is not appropriate for NMSBIC and that GASB-based financial statements would be less informative than financial statements based on the FASB framework. However, continued use of the FASB framework would result in an ‘adverse’ auditors’ opinion because NMSBIC is considered governmental for purposes of accounting and financial reporting.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Change in Financial Reporting Framework – Continued

The 2016 financial statements are presented for comparison. and are unchanged from those issued in the previous year, since adoption of the FRF for SME's did not require changes to the previously issued, FASB based financial statements.

Cash Equivalents

Cash and cash equivalents at June 30, 2017 and 2016, consist of demand deposit accounts and money market deposit accounts held at New Mexico branches of state and national banks.

Investments

NMSBIC reports gains and losses on investments as increases or decreases in temporarily restricted net assets unless their use is permanently restricted by explicit donor stipulations or by law.

For purposes of making equity investments in accordance with the Act, NMSBIC enters into limited partnership agreements (Cooperative Agreements) as a limited partner. Investments are carried at market value as determined in good faith by the general partner of each such limited partnership, in accordance with Cooperative Agreements. The general partners of these limited partnerships determine market value based upon fair value of the underlying investments of the limited partnerships, as there is no ready market for these investments. Realized gains and losses are recorded on a specific identification method upon the sale or write-off of investment assets of the limited partnerships. Investment valuation adjustments are determined by general partners based on an increase or impairment in value in underlying investments during the investment-holding period. Management and operating fees of equity investments are determined by the general partners in accordance with the Cooperative Agreements and are reflected as a decrease in partner capital accounts.

A loan receivable is considered to be past due if any portion of the receivable balance is unpaid and outstanding for more than one month. For the years ended June 30, 2017 and 2016, allowances have been established for loan losses incurred as a result of debt investments made under Cooperative Agreements are as follows:

	<u>2017</u>	<u>2016</u>
Allowance for loan losses, beginning	\$ 176,382	\$ 222,026
Loan losses incurred in current period	(72,328)	(64,256)
Provision for loan losses	<u>63,482</u>	<u>18,612</u>
Allowance for loan losses, ending	<u>\$ 167,536</u>	<u>\$ 176,382</u>

NMSBIC may only make debt and equity investments in New Mexico businesses and in accordance with restrictions imposed by the Act.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Net Asset Classifications

NMSBIC classifies net assets and revenues, expenses, gains and losses based on the existence, or absence, of donor-imposed restrictions. Unrestricted net assets have no donor-imposed restrictions. Revenues that are donor restricted are reported as increases in unrestricted net assets if the restrictions expire in the reporting period in which the revenue is recognized.

Other Program Services

Other program services are comprised of an allocation of management and general expenses directly related to delivery of program services.

Fair Value Measurements

Accounting Standards Codification Topic 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 – Unadjusted quoted prices in active markets for identical investments that NMSBIC has the ability to access at the measurement date.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the investment, either directly or indirectly. These inputs may include quoted prices for the identical instrument in an inactive market, inputs other than observable quoted prices, or inputs derived principally from or corroborated by observable market data by correlation or other means.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Subsequent Events

NMSBIC has evaluated all events occurring subsequent to June 30, 2017 and through September 25, 2017, which is the date that the financial statements were issued, and believes that no events occurring during this period require either recognition or disclosure in the accompanying financial statements.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 2 – CONCENTRATIONS

Concentration of Funding

NMSBIC receives 100% of its funding from the New Mexico Severance Tax Permanent Fund.

Concentration of Credit Risk

NMSBIC maintains its cash and cash equivalent balances in New Mexico branches of state and national financial institutions. The amounts on deposit with these financial institutions are insured by the Federal Deposit Insurance Corporation, are 100% collateralized by government-backed securities, or are 100% secured by a letter of credit from the Federal Home Loan Bank of Cincinnati. NMSBIC has not experienced, and believes it is not exposed to significant credit risk from these deposits.

NMSBIC enters into Cooperative Agreements with parties that have demonstrated the ability to provide business assistance to new and expanding businesses and that are primarily engaged in the business of providing business services and debt and equity capital to new and expanding businesses. Under Cooperative Agreements with lenders, the lenders use their own funds and funds provided by NMSBIC to make loans to new and expanding businesses. Concentrations of credit risk arise from a number of loans made by such third parties utilizing NMSBIC funds to startup businesses. The lenders with which NMSBIC has entered into Cooperative Agreements have discretion as to whether or not to require, and the amount of, collateral taken, on the loans.

NOTE 3 – FAIR VALUE MEASUREMENT

The following table presents the fair value hierarchy for assets measured at fair value on a recurring basis as of June 30, 2017:

<u>Description</u>	<u>Assets at Fair Value</u>			
	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Cooperative loan agreements	\$ 18,378,674	\$ -	\$ 18,378,674	\$ -
Equity investments in New Mexico entities	10,426,049	-	-	10,426,049
Investment held with NM State Investment Council	8,262,462	-	8,262,462	-
	<u>\$ 37,067,185</u>	<u>\$ -</u>	<u>\$ 26,641,136</u>	<u>\$ 10,426,049</u>

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 3 – FAIR VALUE MEASUREMENT – CONTINUED

The following table presents the fair value hierarchy for assets measured at fair value on a recurring basis as of June 30, 2016:

<u>Assets at Fair Value</u>				
<u>Description</u>	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Cooperative loan agreements	\$ 16,876,599	\$ -	\$ 16,876,599	\$ -
Equity investments in New Mexico entities	14,994,617	-	-	14,994,617
Investment held with NM State Investment Council	3,051,478	-	3,051,478	-
	<u>\$ 34,922,694</u>	<u>\$ -</u>	<u>\$ 19,928,077</u>	<u>\$ 14,994,617</u>

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used.

Cooperative loan agreements: Valued at the net asset value of debt investment at year-end.

Equity investments in New Mexico entities: Valued at market value as determined in good faith by the general partner of each such limited partnership.

Investment held with NM State Investment Council: Valued at NMSBIC's percentage share in the pooled fund in which the pooled securities are measured using the closing price of the traded security at the statement of financial position date.

Certificates of Deposit: Valued at face value plus accrued earnings, which approximate fair value.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 3 – FAIR VALUE MEASUREMENT – CONTINUED

Level 3 Investments

The following tables present NMSBIC's activities for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended June 30, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Balance, beginning of year	\$ 14,994,617	\$ 13,896,757
Total gains or losses (realized/unrealized) included in earnings	(874,012)	4,053,723
Operating income and expenses, net	(28,336)	(240,340)
Cash calls and redemptions, net	<u>(3,666,220)</u>	<u>(2,715,523)</u>
Balance, end of year	<u>\$ 10,426,049</u>	<u>\$ 14,994,617</u>

NOTE 4 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are restricted for funding debt or equity investments in accordance with the Act.

Temporarily restricted net assets are restricted for the following purposes:

	<u>2017</u>	<u>2016</u>
Cumulative severance tax permanent fund capital contributions	\$ 47,682,573	\$ 47,682,573
Cumulative return of net excess funds	(2,191,561)	(2,191,561)
Cumulative expenses in excess of other revenues	<u>(7,036,074)</u>	<u>(6,457,496)</u>
	<u>\$ 38,454,938</u>	<u>\$ 39,033,516</u>

Temporarily restricted net assets were released as follows:

	<u>2017</u>	<u>2016</u>
Satisfaction of purpose restrictions	<u>\$ 374,283</u>	<u>\$ 2,778,134</u>

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 5 – STATE INVESTMENT OFFICER COMMITMENT

Prior to July 1, 2007, Section 7-27-5.15 NMSA 1978 required that the State Investment Officer make a commitment to NMSBIC pursuant to the Act to invest three-fourths of one percent of the market value of the New Mexico Severance Tax Permanent Fund. If at any time the commitment fell below that level, further commitments must be made until the invested capital is equal to three-fourths one percent of the market value of the fund. Effective July 1, 2007, the commitment was increased to one percent. Funding received from the State Investment Officer due to the net market value of the New Mexico Severance Tax Permanent Fund was zero in both 2017 and 2016.

NOTE 6 – NET EXCESS FUNDS

Pursuant to Section 58-29-7 NMSA 1978, the NMSBIC shall return to the Severance Tax Permanent Fund an amount equal to the net excess funds held by the NMSBIC. “Net excess funds” are calculated as the return on investments to the corporation in the amounts of dividends and interest actually received plus any capital gains actually realized, less the operating expenses of the NMSBIC and less amounts reasonably reserved for losses. NMSBIC had excess funds of zero and \$2,191,561 as of June 30, 2017 and 2016, respectively, that are required to be returned to the Severance Tax Permanent Fund. The net excess funds are reflected as a liability in the accompanying financial statements.

NMSBIC’s calculations of net excess fund balances as of June 30, 2017 and 2016 are as follows:

	<u>2017</u>	<u>2016</u>
Interest and dividends received, cash basis	\$ 686,567	\$ 404,228
Operating expenses, net of loan losses	(310,804)	(567,957)
Accumulated reserve for debt and equity losses	(1,496,422)	(1,351,626)
Capital gains realized	<u>184,713</u>	<u>3,706,916</u>
Net (deficient) excess funds	<u>\$ (935,946)</u>	<u>\$ 2,191,561</u>

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 7 – INVESTMENTS IN NEW MEXICO ENTITIES

Cooperative Loan Agreements

NMSBIC is party to two loan participation Cooperative Agreements with New Mexico non-profit corporations (ACCION and WESST Corp.). Under these agreements, NMSBIC has made capital commitments to provide revolving funding for loans to be made by these corporations to New Mexico small businesses. For each loan made, these corporations provide 25% of the funding and NMSBIC provides the remaining 75%. Under the participation agreement with WESST Corp., the NMSBIC shares in 75% of loan losses and recoveries. In November 2013, NMSBIC terminated its loan participation agreement with ACCION and entered into a new participation agreement. Loans outstanding under the terminated participation agreement will run off in the normal course of business. The NMSBIC shares in 75% of loan losses and recoveries under the terminated participation agreement. The new agreement limits loan losses that can be passed through to NMSBIC to 1% of the outstanding loan balance during any fiscal year. The terms, pricing, and size of any loan are subject to the discretion of these corporations. These corporations make non-traditional loans. Collateral for the loans may also be non-traditional, or in some cases no collateral at all.

The loans are considered risky and may have a higher rate of default than traditional loans. Loan amounts made under the program are limited under the agreements. These corporations undertake good faith efforts to make loans outside the Albuquerque metropolitan area. Loans are serviced by these corporations, with monthly reports and principal and interest remittances provided to NMSBIC. NMSBIC's agreements with these corporations have no maturity date, but may be terminated by either party upon ninety days written notice, with any loans outstanding at the time of termination handled in the ordinary course of business until the loans are collected or written off. During the years ended June 30, 2017 and 2016, interest income of \$199,949 and \$162,711, respectively, was recognized related to these investments. See supplementary schedules for detail on these agreements.

In December 2013, NMSBIC entered into an unsecured line-of-credit agreement with a New Mexico nonprofit corporation (New Mexico Mortgage Finance Authority, or NMMFA) to provide funds for the development of affordable housing in areas of New Mexico where job growth is restricted by a shortage of such housing. Under this agreement, NMSBIC provides a revolving, unsecured loan to this corporation, which matures in November 2018. NMSBIC does not share in any loan losses or recoveries. Loans are serviced by the corporation, with quarterly reports and principal and interest remittances provided to NMSBIC. The agreement contains provisions that the corporation agrees to maintain a certain level of net assets, and agrees to undertake good faith efforts to make loans outside the Albuquerque metropolitan area.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 7 – INVESTMENTS IN NEW MEXICO ENTITIES – CONTINUED

During the years ended June 30, 2017 and 2016, interest income of \$18,561 and \$18,625, respectively, was recognized related to this investment. See supplementary schedules for detail on this agreement.

NMSBIC is party to a revolving loan Cooperative Agreement with a New Mexico nonprofit corporation (New Mexico Community Development Loan Fund, or NMCDLF). Under this agreement, NMSBIC provides a revolving loan to this corporation, which in turn is fully collateralized by pledged loans. Certain delinquent loans are not eligible to be used as collateral. NMSBIC does not share in any loan losses or recoveries. The agreement includes other provisions under which the corporation has agreed to:

- Maintain certain levels of liquidity, leverage, and net assets
- Limit the maximum loan size under the program
- Restrict loan modifications on nonperforming loans
- Undertake good faith efforts to make loans outside the Albuquerque metropolitan area

Loans are serviced by the corporation, with quarterly reports and principal and interest remittances provided to NMSBIC. The outstanding principal balance of the revolving loan matures in January 2024. Either party can terminate the agreement with 90 days written notice, with the outstanding balance repaid based on balances of collateralized loans. During the years ended June 30, 2017 and 2016, interest income of \$187,248 and \$182,055, respectively, was recognized related to this investment. See supplementary schedules for detail on this agreement.

In September 2014, NMSBIC entered into a line of credit agreement with a New Mexico limited liability company (Rio Vista Growth Capital, LLC or RVGC). Funds provided to RVGC under the terms of the loan agreement will be used to make, acquire, or maintain loans with New Mexico businesses in accordance with the mission and purpose of NMSBIC. Loans are serviced by RVGC, with monthly reports and principal and interest remittances provided to NMSBIC. The outstanding principal balance of the loan matures in August 2021. During the years ended June 30, 2017 and 2016, interest income of \$44,399 and \$42,488, respectively, was recognized related to this investment. Part of the interest is paid quarterly, and the balance is deferred until received by RVGC. Deferred interest receivable was \$54,346 and \$32,446 at June 30, 2017 and 2016, respectively. See supplementary schedules for detail on this agreement.

Equity Cooperative Agreements

NMSBIC is party to several Subscription Agreements and Limited Partnership Agreements under which it has acquired interests as a limited partner in various limited partnerships. Under these agreements, NMSBIC has made capital contribution commitments to provide funding to these limited partnerships to be used for debt or equity investments made in New Mexico small businesses. The limited partnerships have termination dates through 2019. Under the terms of the limited partnership agreements, the partnerships may be extended to dates through 2022. See supplementary schedules for detail on these agreements.

Small Business Investment Corporation

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE 8 – CAPITAL COMMITMENTS

At June 30, 2017, NMSBIC had committed \$45,166,881 of capital through its various debt and equity agreements, of which \$40,073,541 has been called, leaving a remaining commitment of \$5,093,340. At June 30, 2017, NMSBIC has approximately \$1,332,000 of cash-on-hand to immediately handle capital calls. Additionally, NMSBIC has approximately \$8,262,000 invested with the NM State Investment Council in a liquid bond pool as of June 30, 2017. NMSBIC's investment policy allows for capital commitments in excess of capital.

The following table presents capital commitments for each debt and equity agreement as of June 30, 2017:

	Loan and Equity Capital Commitments	Outstanding Loan Balance, Life-to-Date Equity Capital Funded	Remaining Loan and Equity Capital Commitments
Debt Cooperative Agreements			
1. ACCION	\$ 7,750,000	\$ 7,517,796	\$ 232,204
2. NMCDLF	13,000,000	9,373,903	3,626,097
3. WESST CORP	375,000	104,512	270,488
4. NMMFA	1,500,000	800,000	700,000
5. RVGC	750,000	750,000	-
	<u>23,375,000</u>	<u>18,546,211</u>	<u>4,828,789</u>
Equity Cooperative Agreements			
1. Flywheel	1,500,000	1,500,000	-
2. NMCCF	7,000,000	7,000,000	-
3. Verge I	1,800,000	1,800,000	-
4. Verge I.5	3,000,000	3,000,000	-
5. NM Gap Fund I	2,000,000	2,000,000	-
6. NM Mezzanine Fund	2,491,881	2,491,881	-
7. Verge II	3,000,000	2,735,449	264,551
8. Verge II.5	1,000,000	1,000,000	-
	<u>21,791,881</u>	<u>21,527,330</u>	<u>264,551</u>
	<u>\$ 45,166,881</u>	<u>\$ 40,073,541</u>	<u>\$ 5,093,340</u>

SUPPLEMENTARY SCHEDULES

Small Business Investment Corporation

SCHEDULES OF ACTIVITY OF DEBT COOPERATIVE AGREEMENTS

Years Ended June 30, 2017 and 2016

	<u>Loan Commitments</u>	<u>Beginning Gross Loan Balance</u>	<u>Loan Funding Net of Repayments</u>	<u>Realized Loan Loss</u>	<u>Ending Gross Loan Balance</u>	<u>Allowance for Loan Losses</u>	<u>Ending Net Loan Balance</u>
For the year ended June 30, 2017							
1. ACCION #1*	\$ -	\$ 678,490	\$ (386,943)	\$ (10,837)	\$ 280,710	\$ (22,457)	\$ 258,253
2. ACCION #2	7,750,000	5,247,993	2,050,584	(61,491)	7,237,086	(72,371)	7,164,715
3. NMCDLF	13,000,000	9,388,652	(14,749)	-	9,373,903	-	9,373,903
4. WESST CORP	375,000	87,846	16,666	-	104,512	(8,361)	96,151
5. NMMFA	1,500,000	900,000	(100,000)	-	800,000	-	800,000
6. Rio Vista Growth Capital	750,000	750,000	-	-	750,000	(64,348)	685,652
	<u>\$ 23,375,000</u>	<u>\$ 17,052,981</u>	<u>\$ 1,565,558</u>	<u>\$ (72,328)</u>	<u>\$ 18,546,211</u>	<u>\$ (167,537)</u>	<u>\$ 18,378,674</u>
For the year ended June 30, 2016							
1. ACCION #1*	\$ -	\$ 1,393,218	\$ (694,162)	\$ (20,566)	\$ 678,490	\$ (54,279)	\$ 624,211
2. ACCION #2	6,500,000	4,181,614	1,110,069	(43,690)	5,247,993	(52,480)	5,195,513
3. NMCDLF	11,000,000	8,901,360	487,292	-	9,388,652	-	9,388,652
4. WESST CORP	375,000	96,888	(9,042)	-	87,846	(7,027)	80,819
5. NMMFA	1,500,000	512,121	387,879	-	900,000	-	900,000
6. Rio Vista Growth Capital	750,000	750,000	-	-	750,000	(62,596)	687,404
	<u>\$ 20,125,000</u>	<u>\$ 15,835,201</u>	<u>\$ 1,282,036</u>	<u>\$ (64,256)</u>	<u>\$ 17,052,981</u>	<u>\$ (176,382)</u>	<u>\$ 16,876,599</u>

*The ACCION #1 commitment was terminated in 2014 and replaced by ACCION #2. Active loans under the ACCION #1 agreement will run off under their normal course.

Small Business Investment Corporation
SCHEDULES OF ACTIVITY OF EQUITY COOPERATIVE AGREEMENTS
Years Ended June 30, 2017 and 2016

	Investment Capital Commitments	Beginning Investment Fair Value	Cumulative Capital Calls and Redemptions	Realized (Loss) Gain on Investments	Investment Valuation Adjustments	Operating (Expense) Income, net	Ending Investment Fair Value
For the year ended June 30, 2017							
1. Flywheel	\$ 1,500,000	\$ 37,940	\$ -	\$ (87,158)	\$ 82,456	\$ (33,238)	\$ -
2. NMCCF	7,000,000	2,299,090	56,900	(162,155)	(105,895)	(56,983)	2,030,957
3. Verge I	1,800,000	1,369,540	(626,772)	92,906	(302,587)	(17,089)	515,998
4. Verge I.5	3,000,000	2,807,414	(1,332,259)	199,840	(577,448)	(18,483)	1,079,064
5. NM Gap Fund I	2,000,000	3,235,906	-	-	42,228	24,099	3,302,233
6. NMGF II	-	-	-	-	-	-	-
7. NM Mezzanine Fund	2,491,881	855,006	-	-	-	75,197	930,203
8. Verge II	3,000,000	3,344,726	(1,610,487)	141,280	(452,091)	(5,999)	1,417,429
9. Verge II.5	1,000,000	1,044,995	(153,602)	-	254,612	4,160	1,150,165
	<u>\$ 21,791,881</u>	<u>\$ 14,994,617</u>	<u>\$ (3,666,220)</u>	<u>\$ 184,713</u>	<u>\$ (1,058,725)</u>	<u>\$ (28,336)</u>	<u>\$ 10,426,049</u>
For the year ended June 30, 2016							
1. Flywheel	\$ 1,500,000	\$ 200,616	\$ -	\$ (165,035)	\$ 34,828	\$ (32,469)	\$ 37,940
2. NMCCF	7,000,000	3,667,273	(3,277,897)	2,079,512	-	(169,798)	2,299,090
3. Verge I	1,800,000	1,141,319	(97,660)	399,910	(52,136)	(21,893)	1,369,540
4. Verge II.5	3,000,000	2,195,444	(91,158)	847,852	(101,103)	(43,621)	2,807,414
5. NM Gap Fund I	2,000,000	2,403,984	-	(99,953)	953,799	(21,924)	3,235,906
6. NMGF II	-	123,309	(158,328)	23,805	-	11,214	-
7. NM Mezzanine Fund	2,491,881	1,364,024	-	(611,541)	-	102,523	855,006
8. Verge II	3,000,000	2,800,788	(90,480)	1,101,733	(421,134)	(46,181)	3,344,726
9. Verge II.5	1,000,000	-	1,000,000	130,633	(67,447)	(18,191)	1,044,995
	<u>\$ 21,791,881</u>	<u>\$ 13,896,757</u>	<u>\$ (2,715,523)</u>	<u>\$ 3,706,916</u>	<u>\$ 346,807</u>	<u>\$ (240,340)</u>	<u>\$ 14,994,617</u>

See Independent Auditors' Report.

Small Business Investment Corporation

**COMMUNICATION OF
NO MATERIAL WEAKNESSES**

June 30, 2017

September 25, 2017

To the Board of Directors
Small Business Investment Corporation

In planning and performing our audit of the financial statements of the Small Business Investment Corporation, also known as the New Mexico Small Business Investment Corporation (NMSBIC) as of and for the year ended June 30, 2017, in accordance with auditing standards generally accepted in the United States of America, we considered NMSBIC's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of NMSBIC's internal control. Accordingly, we do not express an opinion on the effectiveness of NMSBIC's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of NMSBIC's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

This communication is intended solely for the information and use of management, the Board of Directors, and others within NMSBIC, and is not intended to be, and should not be, used by anyone other than these specified parties.

September 25, 2017


Pulakos CPAs, PC