

**MARYLAND SMALL BUSINESS DEVELOPMENT  
FINANCING AUTHORITY (MSBDF)  
(AN ENTERPRISE FUND OF THE  
STATE OF MARYLAND)**

**Financial Statements Together with  
Report of Independent Public Accountants**

**For the Years Ended June 30, 2013 and 2012**



**SB & COMPANY, LLC**  
EXPERIENCE • QUALITY • CLIENT SERVICE

**JUNE 30, 2013 AND 2012**

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## **REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS**

To the Board of Directors  
Maryland Department of Business and Economic Development

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Maryland Small Business Development Financing Authority (MSBDFA or the Fund), an enterprise fund of the State of Maryland, as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

### **Management's Responsibility for the Financial Statements**

MSBDFA's management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

### **Auditor's 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 auditor's 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 the entity'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 the entity'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.



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## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Fund as of June 30, 2013 and 2012, and the changes in its financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

As discussed in Note 2, the accompanying financial statements present only the transactions of the *Maryland Small Business Development Financing Authority (the Fund)* of the Maryland Department of Business and Economic Development (the Department), and are not intended to present fairly the financial position of the Department or the State of Maryland as of June 30, 2013 and 2012, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental combined statement of net position and combined statement of revenue, expenses and change in net position for the year ended June 30, 2013, is presented for purposes of additional analysis and is not a required part of the basic 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 basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic 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 basic financial statements as a whole.

### *Required Supplemental Information*

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements.



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*Required Supplemental Information (continued)*

We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Hunt Valley, Maryland  
November 22, 2013

*SB & Company, LLC*

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Management's Discussion and Analysis  
June 30, 2013 and 2012**

**Overview of the Financial Statements and Financial Analysis**

In accordance with Governmental Accounting Standards Board (GASB), the Maryland Department of Business and Economic Development (the Department) presents this Management's Discussion and Analysis of the financial statements of the Maryland Small Business Development Financing Authority (MSBDFA or the Fund) for the years ended June 30, 2013 and 2012, as compared to the year ended June 30, 2011.

The report discusses the Statements of Net Position, the Statements of Revenue, Expenses and Change in Net Position, and the Statements of Cash Flows, which together provide an overview of the Fund's activities.

**Statements of Net Position**

The Statements of Net Position present the assets, liabilities, and net position of MSBDFA as of the end of each fiscal year computed in conformity with generally accepted accounting principles. The aim of these statements is to present to the readers a fiscal snapshot of the MSBDFA program. The statements are composed of three major categories namely assets, liabilities, and net position, using the accrual basis of accounting, which is similar to the accounting used by most private sector companies. The Assets section includes the monetary resources owned by the program. Here, assets are classified as current or non-current according to their order of liquidity and timing by which their receipt will be realized. The Liability section of the statements are made up of all the program's debts. The liabilities are classified according to their due date as either current or non-current liabilities. The third category, net position, is the residual interest in the assets of the program that remains after deducting the amount required to satisfy the liabilities. The net position is generally separated into three broad components, namely investments in capital assets - net of related debt, restricted net position, and unrestricted net position.

From the data presented, readers of the statements of net position should be able to reasonably determine the amount of assets available to pay the expenditures necessary to continue the operations of the MSBDFA programs.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDF)**

**Management's Discussion and Analysis  
June 30, 2013 and 2012**

**Statements of Net Position (continued)**

	<u>2013</u>	<u>2012</u>	<u>2011</u>
<b>ASSETS</b>			
Current assets	\$ 19,989,982	\$ 17,031,774	\$ 14,162,088
Non-current assets	<u>1,352,396</u>	<u>3,414,766</u>	<u>4,176,299</u>
<b>Total Assets</b>	<b>21,342,378</b>	20,446,540	18,338,387
<b>LIABILITIES AND NET POSITION</b>			
<b>Total Liabilities</b>	<u>1,996,818</u>	<u>989,344</u>	<u>3,108,002</u>
<b>Net Position</b>			
Net position, restricted - Federal	65,500	65,500	-
Net position, unrestricted	<u>19,280,060</u>	<u>19,391,696</u>	<u>15,230,385</u>
<b>Total Net Position</b>	<b>\$ 19,345,560</b>	<b>\$ 19,457,196</b>	<b>\$ 15,230,385</b>

Current assets increased by \$2,958,208 or 17.4% in fiscal year 2013 compared to fiscal year 2012. Notable factors for the aforementioned change in current assets were driven by an increase in cash in the amount of \$2,473,697 due to the receipts of Maryland legislative insurance revenue of \$2,287,717 as well as an increase in current loan receivable of \$500,603.

Non-current assets in fiscal year 2013 decreased by \$2,062,370 over fiscal year 2012 mainly due to a decrease in loans receivable necessitated by principal repayments exceeding loan disbursements by \$580,825 in fiscal year 2013 as well as an increase in the allowance for loan losses in fiscal year 2013 compared to fiscal year 2012. Additionally, the decrease in investments by \$245,740 in fiscal year 2013 compared to fiscal year 2012 contributed to the decrease in non-current assets.

Current liabilities in fiscal year 2013 increased by \$1,007,474 or 101.8% over fiscal year 2012 primarily as a consequence of an increase in provision for insurance loss in fiscal year 2013 compared to fiscal year 2012.

Unrestricted net position decreased by \$111,636 in fiscal year 2013 compared to fiscal year 2012 as a direct result of culmination of all unrestricted operating activities. Notable factor for the change was driven by the fact that unrestricted general expenses exceeded revenue.

**Statements of Revenue, Expenses and Change in Net Position**

The Statements of Revenue, Expenses, and Change in Net Position are the operating statements for the Maryland Small Business Development Financing Authority. The general components displayed here are operating revenue, operating expenses, non-operating revenue and expenses, fund transfers, change in net position and beginning and ending balances of net position.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Management’s Discussion and Analysis  
June 30, 2013 and 2012**

**Statements of Revenue, Expenses and Change in Net Position (continued)**

The objective of this statement is threefold:

- To present revenue generated by program operations and those received from non-operating activities.
- To show monies expended to operate the program, including losses on bad debts, claims paid as a result of a customer’s default under a loan guaranty or a surety bond, and funds derived from the State Treasury.
- Finally, this statement’s bottom line objective is to display the total change (increase or decrease) in net position during a particular period.

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Operating revenue	\$ 378,662	\$ 473,875	\$ 862,631
Operating expenses	<u>5,423,989</u>	<u>1,616,165</u>	<u>4,436,710</u>
Net operating loss	<b>(5,045,327)</b>	(1,142,290)	(3,574,079)
Non-operating revenue, net	<u>2,433,691</u>	<u>2,869,101</u>	<u>262,037</u>
Net (loss) income before transfer	<b>(2,611,636)</b>	1,726,811	(3,312,042)
Total transfers	<u>2,500,000</u>	<u>2,500,000</u>	<u>2,486,826</u>
Change in net position	<b>(111,636)</b>	4,226,811	(825,216)
Net position, beginning of year	<u>19,457,196</u>	<u>15,230,385</u>	<u>16,055,601</u>
<b>Net Position, End of Year</b>	<u><b>\$ 19,345,560</b></u>	<u><b>\$ 19,457,196</b></u>	<u><b>\$ 15,230,385</b></u>

MSBDFA’s overall financial operating results show the following:

Operating revenue decreased by \$95,213, or 20% during fiscal year 2013, to \$378,662, and operating expenses increased by \$3,807,824 in fiscal year 2013. The decrease in revenue is primarily due to a decrease in the amount of capitalized interest. The increase in expenses is primarily due to a significant increase in the provision for loan and guaranty losses. Non-operating revenue for the year included a general funds appropriation of \$2,500,000, which was the same amount received by the program in fiscal year 2012, and an additional \$2,287,717 from the InvestMaryland tax credit initiative. MSBDFA did not receive any Federal Treasury grant revenue during fiscal year 2013.

Operating revenue decreased by \$388,756, or 45% during fiscal year 2012, to \$473,875 and operating expenses, decreased by \$2,820,545, or 64% in fiscal year 2012, compared to fiscal year 2011. The decrease in revenue is primarily due to a decrease in the amount of capitalized interest. The decrease in expenses is primarily due to a substantial decrease in the provision for loan losses. The annual general funds appropriation was \$2,500,000, which was approximately the same amount received by the program in fiscal year 2011.



**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDF)**

**Management’s Discussion and Analysis  
June 30, 2013 and 2012**

**Statements of Cash Flows**

The Statements of Cash Flows is the third financial statements presented by the Maryland Small Business Development Financing Authority. The purpose of this statement is to provide relevant information about the cash receipts and cash payments of the MSBDF program during the fiscal years ended June 30, 2013 and 2012.

The Statements of Cash Flows classify cash receipts and cash payments of the Fund into four broad components. The major components of the statements are as follows: cash flows from operating activities, cash flows from non-capital financing activities, cash flows from investing activities, and the reconciliation of the net cash flows from operating activities to operating income or loss displayed on the statements of revenue, expenses, and change in net position.

The first component, cash flows from operating activities, is generally the cash effects of transactions and other events that enter into the determination of net income. The second component, cash flows from non-capital financing activities, reflects the cash received and spent for non-operating, non-investing and non-capital purposes. The third component, cash flows from investing activities, deals with cash resulting from purchases, proceeds, and investment interest income. The final component, reconciles net cash provided (used) by operating activities to operating income or loss displayed on the statements of revenue, expenses, and change in net position.

Below is extracted financial data from the statements of cash flows for the years ended June 30, 2013, 2012, and 2011:

	<b>2013</b>	<b>2012</b>	<b>2011</b>
Net cash flows from operating activities	<b>\$ (2,705,734)</b>	\$ (3,663,856)	\$ (2,669,873)
Net cash flows from non-capital financing activities	<b>4,787,717</b>	6,233,000	2,486,826
Net cash flows from investing activities	<b>391,714</b>	115,525	261,236
Net increase in cash	<b>2,473,697</b>	2,684,669	78,189
Cash, beginning of year	<b>15,281,061</b>	12,596,392	12,518,203
<b>Cash, End of Year</b>	<b><u>\$ 17,754,758</u></b>	<b><u>\$ 15,281,061</u></b>	<b><u>\$ 12,596,392</u></b>

Net cash flows from operating activities increased by \$958,122 in fiscal year 2013, compared to a decrease of \$993,983 in fiscal year 2012. The increase in net cash flow from operating activities was primarily due to a decrease in loan disbursements by \$2,753,881 in fiscal year 2013 compared to fiscal year 2012.

Net cash flows from non-capital financing activities decreased by \$1,445,283 in fiscal year 2013 compared to fiscal year 2012. The aforementioned decrease in net cash flows from non-capital financing was primarily due to the fact that no Federal Treasury guaranty funds were received by MSBDF during the year. A total of \$1,485,500 was received during fiscal year 2012.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Management's Discussion and Analysis  
June 30, 2013 and 2012**

**Statements of Cash Flows (continued)**

Net cash flows from investing activities increased by \$276,189 or 239.1% in fiscal year 2013 over the fiscal year 2012 mainly due to increases in the return of investments and investment income in the amounts of \$156,018 and \$148,743, respectively.

Net cash flows from operating activities decreased by nearly \$1,000,000, in fiscal year 2012, compared to a decrease of more than \$2,500,000, in fiscal year 2011, primarily as a result of paying a surety bond claim of nearly \$1,400,000. The programs also experienced a net recovery of loan losses during the year.

Net cash flows from non-capital financing activities increased by \$3,746,174, in fiscal year 2012, primarily due to the receipt of new investment capital by the programs.

**Economic Outlook**

The Department anticipates that MSBDFA will continue to be a primary resource for businesses owned by economically and socially disadvantaged entrepreneurs, and small businesses that do not meet the credit criteria of financial institutions, and consequently are unable to qualify for loans through normal financing channels. The Department anticipates the following performance levels during fiscal year 2014:

Contract Financing - The program projects the approval of sixteen (16) applications during fiscal year 2014. Approximately eleven (11) of these approvals are anticipated to close. The total amount of funds extended is projected to be \$2,200,000.

Guaranty Fund - A total of sixteen (16) loans are projected to be approved during fiscal year 2014. At least twelve (12) are projected to close, requiring the commitment of program funds of approximately \$2,500,000.

Surety Bond Fund - The program projects the approval of approximately \$8,000,000, during fiscal year 2014 to facilitate bonding for thirteen (13) businesses. Approximately eleven (11) transactions are projected to settle and provide an estimated \$5,800,000 of assistance.

Equity Participation Investment Program - The program projects approval of thirteen (13) applications during FY 2014. Ten (10) transactions are anticipated to settle during the fiscal year requiring the commitment of approximately \$2,000,000 of financial assistance.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Statements of Net Position  
As of June 30, 2013 and 2012**

	<u>2013</u>	<u>2012</u>
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash	\$ 17,754,758	\$ 15,281,061
Loans receivable, net of allowance of \$167,847 and \$22,811, respectively	2,185,413	1,684,810
Accrued interest receivable	49,811	65,903
<b>Total Current Assets</b>	<u>19,989,982</u>	<u>17,031,774</u>
<b>Non-Current Assets</b>		
Loan receivable, net of current portion and allowance of 742,410 and \$61,038, respectively	607,252	2,423,882
Investments	745,144	990,884
<b>Total Non-Current Assets</b>	<u>1,352,396</u>	<u>3,414,766</u>
<b>Total Assets</b>	<u>21,342,378</u>	<u>20,446,540</u>
<b>LIABILITIES AND NET ASSETS</b>		
<b>Current Liabilities</b>		
Accounts payable	-	24,375
Unearned insurance fees	17,799	35,153
Reserve for guaranty losses	1,938,219	929,816
Reserve for guaranty losses - Federal	40,800	-
<b>Total Liabilities</b>	<u>1,996,818</u>	<u>989,344</u>
<b>Net Position</b>		
Restricted - Federal	65,500	65,500
Unrestricted	19,280,060	19,391,696
<b>Total Net Position</b>	<u>\$ 19,345,560</u>	<u>\$ 19,457,196</u>

The accompanying notes are an integral part of these financial statements.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Statements of Revenue, Expenses, and Change in Net Position  
For the Years Ended June 30, 2013 and 2012**

	<u>2013</u>	<u>2012</u>
<b>Operating Revenue</b>		
Interest income on loans receivable	\$ 139,566	\$ 95,348
Insurance/guarantee fees	109,201	127,266
Recoveries	11,096	36,059
Capitalized interest	91,206	211,551
Other income	27,593	3,651
<b>Total Operating Revenue</b>	<u>378,662</u>	<u>473,875</u>
<b>Operating Expenses</b>		
Management fees	1,556,693	1,410,872
Other direct expenses	261,687	40,938
Administrative allocations	681,296	870,707
Provision for loan losses	826,408	46,719
Provision for guarantee losses	2,097,905	(753,071)
<b>Total Operating Expenses</b>	<u>5,423,989</u>	<u>1,616,165</u>
<b>Net Operating Loss</b>	<u>(5,045,327)</u>	<u>(1,142,290)</u>
<b>Non-Operating Revenue</b>		
Decrease in fair value of investments	(89,722)	(979,423)
Federal treasury grant revenue	-	1,485,500
Invest Maryland grant revenue	2,287,717	2,247,500
Investment income	235,696	115,524
<b>Total Non-Operating Revenue, net</b>	<u>2,433,691</u>	<u>2,869,101</u>
<b>Net (Loss) Income Before Transfers</b>	<u>(2,611,636)</u>	<u>1,726,811</u>
<b>Transfers</b>		
State appropriation	<u>2,500,000</u>	<u>2,500,000</u>
Change in net position	(111,636)	4,226,811
Net position, beginning of year	19,457,196	15,230,385
<b>Net Position, End of Year</b>	<u>\$ 19,345,560</u>	<u>\$ 19,457,196</u>

The accompanying notes are an integral part of these financial statements.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDF)**

**Statements of Cash Flows  
For the Years Ended June 30, 2013 and 2012**

	<u>2013</u>	<u>2012</u>
<b>Cash Flows from Operating Activities</b>		
Interest income on loans receivable	\$ 155,658	\$ 118,958
Insurance/guarantee fees	91,847	125,547
Recoveries	11,096	36,059
Other income	27,593	3,651
Loans receivable disbursements	(4,625,085)	(7,378,966)
Accounts payable	(24,375)	-
Proceeds from collection of principal on loans receivable	5,205,910	7,117,280
Management service fees	(1,556,693)	(1,386,497)
Other direct expenses	(261,687)	(40,938)
Administrative allocations	(681,296)	(870,707)
Claims paid	(1,048,702)	(1,388,243)
<b>Net Cash Flows from Operating Activities</b>	<u>(2,705,734)</u>	<u>(3,663,856)</u>
<b>Cash Flows from Non-Capital Financing Activities</b>		
Invest Maryland grant revenue	2,287,717	2,247,500
State general fund appropriation	2,500,000	2,500,000
Federal grant revenue	-	1,485,500
<b>Net Cash Flows from Non-Capital Financing Activities</b>	<u>4,787,717</u>	<u>6,233,000</u>
<b>Cash Flows from Investing Activities</b>		
Interest income	86,953	115,525
Investment income	148,743	-
Return of investment	156,018	-
<b>Net Cash Flows from Investing Activities</b>	<u>391,714</u>	<u>115,525</u>
Net increase in cash	2,473,697	2,684,669
Cash, beginning of year	15,281,061	12,596,392
<b>Cash, End of Year</b>	<u>\$ 17,754,758</u>	<u>\$ 15,281,061</u>
<b>Reconciliation of Operating Loss to Net Cash from Operating Activities</b>		
Operating loss	\$ (5,045,327)	\$ (1,142,290)
Provision for loan losses	826,408	46,719
Capitalized interest	(91,206)	(211,551)
Provision for guarantee losses	2,097,905	(753,071)
Effect of net changes in non-cash assets and liabilities:		
Loans receivable	580,825	(261,686)
Accounts payable	(24,375)	24,375
Accrued interest	16,092	23,611
Reserve for guarantee losses	(1,048,702)	(1,388,243)
Unearned insurance premiums and issuance fees	(17,354)	(1,720)
<b>Net Cash from Operating Activities</b>	<u>\$ (2,705,734)</u>	<u>\$ (3,663,856)</u>
<b>Supplemental Disclosure for Non-Cash Transactions</b>		
Capitalized interest added to loans receivable	<u>\$ 91,206</u>	<u>\$ 211,551</u>

The accompanying notes are an integral part of these financial statements.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**1. AUTHORIZING LEGISLATION**

The Maryland Small Business Development Financing Authority (MSBDFA or the Fund) was established by the State of Maryland in 1978 and is governed by the Economic Development Article and the MSBDFA programs are contained in Sections 5-501 through 5-575. MSBDFA is administered by the Department of Business and Economic Development (the Department). MSBDFA's purpose is to assist socially or economically disadvantaged entrepreneurs and small businesses in the creation and expansion of Maryland businesses. The programs can extend financial assistance to small businesses that are unable to obtain adequate business financing on reasonable terms through normal financing channels.

During the 2002 session of the Maryland General Assembly, the statutes concerning eligibility were broadened to include businesses other than those that are determined to be socially or economically disadvantaged. More specifically, the new law allowed MSBDFA to extend financial assistance to small businesses that are unable to obtain adequate business financing on reasonable terms through normal financing channels.

MSBDFA currently offers assistance through the following programs:

- *Contract Financing Fund Program* - This program offers financial assistance through direct loans and guarantees of loans to provide working capital to eligible businesses to complete work on contracts, for which the majority of funding is provided by Federal, state or local government agencies or utilities regulated by the Public Service Commission.
- *Long-Term Guaranty Fund Program* - This program offers financial institutions loan guarantees and payments of interest subsidies on loans made to eligible businesses to be used for working capital, the acquisition of machinery and equipment and real property (if such property is to be used in the applicant's business) and improvements to real property owned or leased by the applicant.
- *Surety Bond Fund Program* - Under this program, MSBDFA provides bonding assistance to eligible small businesses to qualify for and complete work on contracts, for which the majority of funding is provided by state or local government agencies or utilities regulated by the Public Service Commission. The Program may also provide assistance for contracts with private entities that display the financial capacity to fund a proposed contract. MSBDFA can directly issue bid, performance or payment bonds or guaranty a surety's losses incurred as a result of the contractor's breach of a bid, performance, or payment bond.
- *Equity Participation Investment Program (EPIP)* - This program was created with the explicit purpose of encouraging and aiding in the creation, development, expansion, and retention of franchises, technology-based and other traditional businesses and in the acquisition of existing businesses to be located in Maryland. The EPIP provides equity investments, loans and loan guarantees to achieve its objectives.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFDA)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reporting Entity**

MSBDFDA is an enterprise fund of the State of Maryland.

**Basis of Presentation**

The GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre- November 30, 1989 FASB and AICPA Pronouncements*, in December 2010, effective for financial statement periods beginning after December 15, 2011. In November 2010, the GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, and Statement No. 61, *The Financial Reporting Entity: Omnibus – an amendment of GASB Statements No. 14 and No. 34*, effective for periods beginning after December 15, 2011 and June 15, 2012, respectively. In addition, in June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, effective for periods beginning after December 15, 2011. The Fund has implemented the above GASB statements, and they have no material effect on the financial position of the Fund.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management of MSBDFDA to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies as of the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**Relationship with the Department**

MSBDFDA is one of many programs administered by the Department. MSBDFDA has no direct employees and are entirely supported by staff at the Department to perform all necessary functions of MSBDFDA. The Department allocated certain operating, general, and administrative costs to MSBDFDA, which is the Department's estimate of its cost to manage and administer MSBDFDA's operations. This allocation from the Department is not necessarily representative of MSBDFDA's cost as if it was a stand-alone entity and could significantly change in the future.

MSBDFDA's accompanying financial statements are not indicative of MSBDFDA as if it were a stand-alone entity.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Loans Receivable**

Loans receivable are stated at the amount of unpaid principal, reduced by an allowance for loan losses. Loans that are due within one year are classified as current assets, and all other loans are classified as non-current assets. Interest on loans is calculated using the simple interest method on daily balances of the principal amount outstanding. The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans that may become uncollectible because of present conditions, based on evaluations of the collectability of loans and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, portfolio quality, review of specific problems regarding the loans, and current economic conditions that may affect the borrower's ability to pay. The allowance for loan losses is based on estimates, and ultimate losses may vary from the current estimates. The allowance for loan losses has been allocated between current and non-current loan balances.

These estimates are reviewed periodically and, as adjustments become necessary, they are reported through the provision for loan losses in the periods in which they become known. Accrual of interest is discontinued on a loan when management believes that, after considering economic and business conditions and collection efforts, the borrower's financial condition is such that collection of interest is doubtful.

**Reserve for Guarantee Losses**

MSBDFA has provided partial guarantees on loans and bonds. Outstanding guarantees range from 48% to 100% of the outstanding loan and bond balances. The reserve for guaranty losses is estimated to provide losses on existing insured loans. The amount of such reserve is estimated based on a continuing review of outstanding guarantees, loss experience, and estimated liquidation values of underlying collateral and economic conditions, which may affect each borrower's ability to pay. Such estimates are susceptible to change in the near term due to changing economic conditions, the value of the collateral and paying capacity of the borrower and, where applicable, guarantors. Therefore, actual results could differ significantly from those estimates.

**Unearned Insurance Fees**

Unearned Insurance fees represent premiums paid for loan guaranty insurance that has not been earned. Revenue is recognized monthly on a straight-line basis.



**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFA)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**3. CASH**

Cash receipts and disbursements of the Fund are made through a cash pool maintained by the State Treasurer. The State Treasurer has statutory responsibility for the State's cash management activities. The State Treasurer maintains these and other State agency funds on a pooled basis in accordance with State statutes. For additional information on the risk of cash, see the State of Maryland Comprehensive Annual Financial Report (CAFR). Listed below is information related to the State's cash pool.

**Interest Rate Risk**

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Fund adheres to the State Treasurer's policy for managing its exposure to fair value loss arising from increasing interest rates.

The State Treasurer's investment policy states that to the extent possible, it will attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the State Treasurer will not directly invest in securities maturing more than five years from the date of purchase.

**Credit Risk**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Fund's policy for reducing its exposure to credit risk is to comply with the State Treasurer's policy, which requires that the State Treasurer's investments in repurchase agreement be collateralized by U.S. Treasury and agency obligations. In addition, investments may be made directly in U.S. Treasury or agency obligations.

**Concentration of Credit Risk**

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The Fund's policy for reducing this risk of loss is to comply with the State Treasurer's policy, which limits the amount of repurchase agreements to be invested with a particular institution to 30% of the portfolio. Otherwise, there is no limit on the amount that may be invested in any one issuer.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDF)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**3. CASH (continued)**

**Custodial Credit Risk - Deposits**

Custodial credit risk is the risk that, in the event of a bank failure, the Fund's deposits may not be returned to it. Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are (a) uncollateralized, (b) collateralized with securities held by the pledging financial institution, or (c) collateralized with securities held by the pledging financial institution's trust department or agent but not in the Fund's name. The Fund does not have a formal deposit policy for custodial credit risk, but follow the State Treasurer's policy which states that the State Treasurer may deposit in a financial institution in the State, any unexpended or surplus money in which the State Treasurer has custody. As of June 30, 2013 and 2012, all of the Fund's cash was deposited with the State Treasury and this was not subject to custodial risk.

**4. LOANS RECEIVABLE**

Loans receivable as of June 30, 2013 and 2012, are summarized as follows:

	<b>2013</b>	<b>2012</b>
Loans receivable, beginning of year	\$ <b>4,192,541</b>	\$ 3,886,254
Loan disbursements	<b>4,625,085</b>	7,378,966
Capitalized interest income	<b>91,206</b>	-
Proceeds from collections	<b>(5,205,910)</b>	(7,072,679)
<b>Loans Receivable, End of Year</b>	<b>\$ 3,702,922</b>	<b>\$ 4,192,541</b>

Activities in the allowance for loan losses for the years ended June 30, 2013 and 2012, were as follows:

	<b>2013</b>	<b>2012</b>
Balance, beginning of year	\$ <b>83,849</b>	\$ 204,080
Loans written off	-	(166,950)
Allowance for loan loss	<b>826,408</b>	46,719
<b>Balance, End of Year</b>	<b>\$ 910,257</b>	<b>\$ 83,849</b>

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFa)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**5. INVESTMENTS**

MSBDFa provides loan and equity investments to small businesses through the Equity Participation Investment Program (EPIP). The values of these investments are stated at fair value. Management assesses investments for impairment based on financial condition, operating results and other factors on an annual basis. Based on the fair value analysis of investment activity, management has adjusted the value of MSBDFa investments' portfolio assets from \$990,884 to \$745,144 as a direct result of depreciation in the fair value of its investments as of June 30, 2012 and 2013, respectively. MSBDFa made no new investments during fiscal years 2013 and 2012. MSBDFa had a return on its investments of \$156,018 for June 30, 2013 and return on its investments for June 30, 2012.

<u>Security</u>	<u>Cost</u>	<u>Beginning Fair Value 7/1/2012</u>	<u>Appreciation (Depreciation)</u>	<u>Ending Fair Value 6/30/2013</u>
MidAtlantic	\$ 500,000	\$ 500,000	\$ -	\$ 500,000
MidAtlantic Metro Broadband	394,600	194,973	-	194,973
MidAtlantic Metro Broadband	62,956	31,107	-	31,107
Navtrak, Inc.	250,000	203,109	(28,027)	19,064
Odyssey Technologies, Inc.	562,751	-	-	-
Odyssey Technologies, Inc.	200,000	61,695	(61,695)	-
<b>Total</b>	<u>\$ 1,970,307</u>	<u>\$ 990,884</u>	<u>\$ (89,722)</u>	<u>\$ 745,144</u>

**6. RESERVE FOR GUARANTY LOSSES**

A summary of outstanding loans and bonds and the applicable insurance as of June 30, 2013, and 2012, were as follows:

	<u>2013 Original Balance</u>	<u>2013 Outstanding Balance</u>	<u>2012 Original Balance</u>	<u>2012 Outstanding Balance</u>
Loans and bonds	<u>\$ 34,510,307</u>	<u>\$ 26,772,609</u>	<u>\$ 40,680,807</u>	<u>\$ 30,895,754</u>
Insurance	<u>\$ 6,929,450</u>	<u>\$ 5,916,241</u>	<u>\$ 9,083,520</u>	<u>\$ 7,394,674</u>

The maximum exposure to MSBDFa, including available borrowing under lines of credit agreements as of June 30, 2013 and 2012, was \$21,654,640 and \$24,707,220, respectively.

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY  
(MSBDFa)**

**Notes to the Financial Statements  
June 30, 2013 and 2012**

**6. RESERVE FOR GUARANTY LOSSES (continued)**

Changes in the reserve for guaranty losses for the years ended June 30, 2013, and 2012, were as follows:

	<u>2013</u>	<u>2012</u>
Balance, beginning of year	\$ 929,816	\$ 3,071,130
Claim payment	(1,048,702)	(1,388,243)
Provision for guaranty losses	2,097,905	(753,071)
<b>Balance, End of Year</b>	<u><u>\$ 1,979,019</u></u>	<u><u>\$ 929,816</u></u>

**7. MANAGEMENT AGREEMENT**

The Department has entered into a contract with Meridian Management Group, Inc. (MMG), a Maryland corporation, to provide management services to MSBDFa. Such services include marketing and public relations, underwriting, loan closing, and certain loan administration. MSBDFa retains approval authority over all proposed transactions under its different programs, and the Department will continue to provide certain accounting and administrative functions subsequent to loan closing. During the year ended June 30, 2012, the Department exercised its option to extend the management contract with MMG for an additional five-year period. Minimum annual future payments on this contract, which expires on June 30, 2017, are approximately \$1.46 million, including monitoring fees.

**8. PENSION AND OTHER POSTEMPLOYMENT BENEFITS**

Eligible employees who perform services for MSBDFa and employees of the State are covered under the retirement plans of the State Retirement and Pension System of Maryland (System) and are also entitled to certain healthcare benefits upon retirement. MSBDFa's only liability for retirement and post-employment benefits is its required annual contribution to the Department, which in turn was paid in full to the State of Maryland prior to year end. The System is considered part of the State's financial reporting entity, and is not considered a part of MSBDFa's reporting entity. The System prepares a separate Comprehensive Annual Financial Report, which can be obtained from the State Retirement and Pension System of Maryland at 120 East Baltimore Street, Baltimore, Maryland 21202.

**SUPPLEMENTARY INFORMATION**

**MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY (MSBDFA)**

**Combined Statement of Net Position  
As of June 30, 2013, with Comparative Total for 2012**

	<u>Contract Financing Fund</u>	<u>Long-Term Guaranty Fund</u>	<u>Federal Guaranty Fund</u>	<u>Surety Bond Fund</u>	<u>EPIP Fund</u>	<u>Invest MD EPIP Fund</u>	<u>Total 2013</u>	<u>Total 2012</u>
<b>ASSETS</b>								
Cash	\$ 2,670,265	\$ 2,196,719	\$ 1,253,067	\$ 5,006,613	\$ 2,149,064	\$ 4,479,030	\$ 17,754,758	\$ 15,281,061
Loans receivables, net	919,264	-	-	-	1,873,401	-	2,792,665	4,108,692
Accrued interest receivable	4,716	-	-	-	45,095	-	49,811	65,904
Investments	-	-	-	-	745,144	-	745,144	990,884
<b>Total Assets</b>	<u>3,594,245</u>	<u>2,196,719</u>	<u>1,253,067</u>	<u>5,006,613</u>	<u>4,812,704</u>	<u>4,479,030</u>	<u>21,342,378</u>	<u>20,446,541</u>
<b>LIABILITIES AND NET ASSETS</b>								
<b>Liabilities</b>								
Accounts payable	-	-	-	-	-	-	-	24,376
Unearned insurance premiums	-	16,817	982	-	-	-	17,799	35,152
Reserve for guaranty losses	-	1,750,542	40,800	187,677	-	-	1,979,019	929,816
<b>Total Liabilities</b>	<u>-</u>	<u>1,767,359</u>	<u>41,782</u>	<u>187,677</u>	<u>-</u>	<u>-</u>	<u>1,996,818</u>	<u>989,344</u>
<b>Net Position</b>								
Unrestricted net position	3,594,245	429,360	1,145,785	4,818,936	4,812,704	4,479,030	19,280,060	19,457,196
Restricted Federal	-	-	65,500	-	-	-	65,500	-
<b>Total Net Position</b>	<u>\$ 3,594,245</u>	<u>\$ 429,360</u>	<u>\$ 1,211,285</u>	<u>\$ 4,818,936</u>	<u>\$ 4,812,704</u>	<u>\$ 4,479,030</u>	<u>\$ 19,345,560</u>	<u>\$ 19,457,196</u>

MARYLAND SMALL BUSINESS DEVELOPMENT FINANCING AUTHORITY (MSBDFA)

Combined Statement of Revenue, Expenses, and Change in Net Position  
For the Year Ended June 30, 2013, with Comparative Total for 2012

	Contract Financing Fund	Long-Term Guaranty Fund	Federal Guaranty Fund	Surety Bond Fund	EPIP Fund	Invest MD EPIP Fund	Total 2013	Total 2012
<b>Operating Revenue</b>								
Interest revenue	\$ 56,546	\$ -	\$ -	\$ -	\$ 33,209	\$ -	\$ 89,755	\$ 29,444
Accrued interest income	4,716	-	-	-	45,095	-	49,811	65,904
Loan recoveries	3,500	-	-	-	7,596	-	11,096	36,059
Guaranty/insurance premiums	-	88,265	8,171	12,765	-	-	109,201	127,266
Other income	3,008	-	-	-	24,585	-	27,593	3,651
Capitalized interest	-	-	-	-	91,206	-	91,206	211,551
<b>Total Operating Revenue</b>	<b>67,770</b>	<b>88,265</b>	<b>8,171</b>	<b>12,765</b>	<b>201,691</b>	<b>-</b>	<b>378,662</b>	<b>473,875</b>
<b>Operating Expenses</b>								
Miscellaneous	875	875	-	875	875	-	3,500	10,150
Contractual expenses	64,517	61,371	3,144	64,517	64,638	-	258,187	30,788
Administrative expenses	170,324	170,324	-	170,324	170,324	-	681,296	870,707
MSBDFA management fee	375,126	253,272	121,855	375,127	375,126	56,187	1,556,693	1,410,872
Loan loss expense	144,966	-	-	-	681,442	-	826,408	46,719
Provision for guaranty insurance losses	-	1,464,994	40,800	592,111	-	-	2,097,905	(753,071)
<b>Total Operating Expenses</b>	<b>755,808</b>	<b>1,950,836</b>	<b>165,799</b>	<b>1,202,954</b>	<b>1,292,405</b>	<b>56,187</b>	<b>5,423,989</b>	<b>1,616,165</b>
<b>Net Operating Loss</b>	<b>(688,038)</b>	<b>(1,862,571)</b>	<b>(157,628)</b>	<b>(1,190,189)</b>	<b>(1,090,714)</b>	<b>(56,187)</b>	<b>(5,045,327)</b>	<b>(1,142,290)</b>
<b>Non-Operation Revenue</b>								
Federal grant revenue	-	-	-	-	-	-	-	1,485,500
Invest Maryland grant revenue	-	-	-	-	-	2,287,717	2,287,717	2,247,500
Investment interest income	14,450	21,854	-	28,006	22,643	-	86,953	115,524
Investment income	-	-	-	-	148,743	-	148,743	-
Increase (Decrease) in fair value of investments	-	-	-	-	(89,722)	-	(89,722)	(979,423)
<b>Total Non-Operating Revenue</b>	<b>14,450</b>	<b>21,854</b>	<b>-</b>	<b>28,006</b>	<b>81,664</b>	<b>2,287,717</b>	<b>2,433,691</b>	<b>2,869,101</b>
<b>Net (Loss) Income Before Transfers</b>	<b>(673,588)</b>	<b>(1,840,717)</b>	<b>(157,628)</b>	<b>(1,162,183)</b>	<b>(1,009,050)</b>	<b>2,231,530</b>	<b>(2,611,636)</b>	<b>1,726,811</b>
<b>Transfers</b>								
State appropriation	500,000	500,000	-	1,000,000	500,000	-	2,500,000	2,500,000
<b>Total Transfers</b>	<b>500,000</b>	<b>500,000</b>	<b>-</b>	<b>1,000,000</b>	<b>500,000</b>	<b>-</b>	<b>2,500,000</b>	<b>2,500,000</b>
Changes in net position	(173,588)	(1,340,717)	(157,628)	(162,183)	(509,050)	2,231,530	(111,636)	4,226,811
Net position, beginning of year	3,767,833	1,770,077	1,368,913	4,981,119	5,321,754	2,247,500	19,457,196	15,230,385
<b>Net Position, End of Year</b>	<b>\$ 3,594,245</b>	<b>\$ 429,360</b>	<b>\$ 1,211,285</b>	<b>\$ 4,818,936</b>	<b>\$ 4,812,704</b>	<b>\$ 4,479,030</b>	<b>\$ 19,345,560</b>	<b>\$ 19,457,196</b>