



Tech Futures:
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By [Michael Volker](#)

Budgets' Impact on Techs, VC Update, Capital Pool Corps Update and VEF Events

Budgets' Impact on Techs

Both the B.C. and Federal governments brought in new budgets last month which contained some good news - while still leaving some unfulfilled wishes - for technology companies.

In the "Innovation and Learning" category, Finance Minister **John Manley** called for Canada to be a "Northern Tiger" - attracting talent and investment to build a knowledge economy.

To its credit, our government is heavily committed to post-secondary education and the development of our research infrastructure. The awarding of research grants to some 2400+ projects and the creation of 2,000 Canada Research Chairs will help build the foundation for a knowledge-based economy.

Furthermore, the research ante (i.e. funding to the research granting councils and hence to universities) has been upped by \$125 million per year. And another \$500 million has been committed to the **Canada Foundation for Innovation** for infrastructure (i.e. funding for research hospitals).

Substantial support is being given to students at all levels - through improvements to the student loans program and grad student scholarships as well as \$41 million to help new Canadians in contributing to the talent pool.

Having a strong education and research base is essential for developing a knowledge-based economy. But, for that knowledge to be transformed into products and services - hence increasing our GDP - requires entrepreneurs and capital. It's in this latter category that we still have a problem and in this regard the Feds still need to do more.

There was nothing new in the budget that gives me any hope that more of the know-how developed at our universities and research institutions can make it past the first stages of commercialization - i.e. the pre-venture financing stages of company development.

There are a few, relatively small, positive Federal announcements that bode well for business investment. These are the RRSP contribution limit increase, the small business tax deduction limit increase, elimination of the capital tax and more funding for seed investments.

The RRSP contribution limit will increase to \$18,000 (from \$13,500) by the year 2006. This is good for entrepreneurs because it will increase the flow of capital to them in building their businesses and secondarily, it's good for them personally because they have to look after their own retirement interests rather than relying on corporate pensions. When the RRSP is stacked with other incentives (read on - as I discuss a great British Columbia vehicle for doing exactly this), it can make a healthy difference.

Perhaps, though, what's really needed is more investor education in the RRSP department. I can't believe how few Canadians capitalize on this great perk. In 2001, 6.2 million Canadian tax filers

contributed just over \$28.4 billion to their RRSPs. The median contribution in 2001 was \$2,600. 83% of tax filers had "contribution room", i.e. they could have contributed more if they wished to. In dollar terms, the \$28.4 billion that was contributed is only 9% of the \$316 billion that was available to tax payers! In 1999, 55% of families had RRSPs, almost double the percentage from 1984. In 1999, the median value of RRSPs was \$20,000 whereas the average size was \$51,200. So there!

As for the small business tax rate, all profitable small businesses (that leaves out many tech companies but nonetheless is a goal that all aspire to achieve - and hence may be more of a motivator than anything else). In any event, for more than 20 years, the Federal tax rate for small business has been set at 12% - BUT only on the first \$200,000 of profit. That has now been lifted to \$300,000. Hey - every little bit helps!

More importantly, the capital tax has been eliminated. This tax has hurt growing companies that need to raise capital to expand. No longer.

The government is also investing directly in small business through an investment of \$190 million in equity capital managed by the **Business Development Bank**. As long as the BDC figures out how to invest this at early stages (without traditional VC-style guidelines and criteria), it might be very useful.

What's missing in the budget, in my opinion, is something to address the the early-stage financing gap. That's the one that let's entrepreneurs mine the intellectual property at universities and produce prototypes that will ultimately lead to VC-bankable deals. The best way to do this is to let those who know (e.g. technology angels) how to do it take risks more willingly. How? Easy - if I put \$100K into a project and it fails after several years, I get a \$100K write-off. Well, why not assume that the project will fail (c'mon - let's face it - most do!) and let me take the write-off immediately (giving me an immediate and attractive re-capture). Then, on those bets that do pay off I'll pay full tax on a zero-cost base investment. Neat, huh?

Now, on to the B.C. budget introduced within a few hours of the federal one, also on Feb 18th. Because of B.C.'s deficit, spending obviously has to be restrained. This, coupled with the Liberals' oft-stated aversion to "subsidize" industry left me unsurprised that that there were no programs or initiatives to stimulate the commercialization process such as seed or prototyping funding support as has flowed in the past to organizations like the **Science Council of B.C.** and the **B.C. Advanced Systems Institute**.

What B.C. did do, though, was to make a very positive step towards stimulating private equity investments through an overhaul of the **Small Business Venture Capital Act** - especially the **Venture Capital Company (VCC)** plan under the **Equity Capital Program**.

Todd Tessier and his colleagues in the **Ministry of Competition, Science and Enterprise** are doing some excellent missionary work in improving and promoting this program.

Under the VCC program, investors can set up a VCC holding company which would invest in a (or several) company. The investors in the VCC would get a 30% *refundable* tax credit from the Province. Since 1985, more than \$400M has been raised in this manner for 575 small enterprises including successful companies such as **ALI Technologies** and **Sierra Wireless Inc.**

The main problem with this program has been the cost associated with setting up, and maintaining, a VCC corporation. There is also a total tax credit limit imposed on the program (\$15 million last year).

Although there are many fine points to this program - which I won't go into here - there have been some substantial improvements. These include an increase in the tax credit ceiling, less red tape, and most importantly - allowing investors to invest directly in a company without having to set up a special VCC - and still get the 30% tax credit.

A special \$5M in credits has been reserved for "New Media" companies - thereby encouraging investment in this particular subsector.

Now, the total tax credits available to B.C. investors add up to \$20 million. This includes the \$5 million New Media allocation. These tax credits represent annual program investment capacity of \$67M per year. Details on this program can be found at the **Ministry of Competition, Science and Enterprise's** web site at: <http://www.bcinbusiness.gov.bc.ca>.

Now here's a great deal for tech company investors: Combine the Federal RRSP program with the Provincial VCC program and you can invest 30-cent dollars in promising new startup enterprises. That's darn good leverage if you ask me. Put \$10K into a tech company and then put the tech company shares into your RRSP. That'll give you \$3K back from B.C. and about \$4K+ (depending on you marginal tax rate) from the Feds. Your exposure is only \$3K - not bad, eh?

There's only a minor glitch in doing this: A small problem with self-administered RRSP plans is that the trustees of these plans (brokerage firms, banks, trust companies, etc) are loathe to accept private equity investments in individuals' plans. This is terrible. And those that do, charge high fees for doing so. What's needed is a better way (hey - is there an opportunity here?) for individual investors (eg family, friends, angels for entrepreneurs) to put their startup portfolios into their self-administered RRSPs.

Other than the VCC improvements, the B.C. budget had little in the way of specific new tech sector benefits.

VC Update

In my [last column](#), I talked about financing sources and reviewed last year's activity on the angel, Venture Capital, private equity and juniorpubco financing fronts.

I didn't have all the final numbers on institutional Venture Capital investing in B.C. In the meantime, **Mary MacDonald & Associates** recently released the 2002 numbers. They report that venture capital investment in Canada continued to fall last year from the levels seen during the tech-market boom, dropping 35 per cent to \$2.5-billion from \$3.8-billion in 2001.

The final number for B.C. was \$251 million - using their criteria which appear to have excluded certain financings such as the approximately \$150 million placement in **Ballard** at the end of the year. This \$251 figure is slightly higher than the \$170 to \$200 million that was reported in the column.

At a seminar that I attended last week, this number was being touted as "the total of all investments in B.C. tech companies". CAUTION: That's simply not the case. Venture Capital investment is only a portion of all investing activity. One must not forget angel investing (a growing force), private equity capital, and public investors who invest in juniorpubcos. The V.C. total is LESS THAN HALF of the grand total. I base this only on the visible and reported data that's readily available. We also know that there's a lot of unreported investing activity - numbers that aren't tracked anywhere.

Capital Pool Corporation (CPC) Comments and Update

In this column, I keep track of Capital Pool Corporation ("CPC") companies as defined by the **TSX Venture Exchange** (the former CDNX) because they may provide funding and management to, and in the process acquire, technology companies. They provide companies with an alternative to traditional venture capital financing. It lets the public investor get into the game. At the February Vancouver Enterprise Forum presentation, the TSX Venture Exchange's president, **Linda Hohol**, identified the CPC program as one of three routes by which an emerging company could become a publicly listed company. The other two were the conventional Initial Public Offering (IPO) and

the Reverse-Take-Over of an existing public "shell". In essence, a CPC deal is like an RTO but usually "cleaner" and simpler.

Check our [Capital Pool Corporation chart](#) (in .pdf format) for a complete list of the TSX-Venture Exchange's CPC companies, thanks to David Ing of Pacific International Securities. This list is updated on a regular basis. It is now current to the end of February, 2003.

New additions to the list since the Dec, 2002 update are: **Arrabbiata Capital Corp.** (from B.C.), **Innovotech Inc.** (from Alberta), **Ore-Leave Capital Inc.** (from Ontario) and **Vinson Biotech Inc.** (from Manitoba). It's nice to see other companies in other provinces starting CPCs.

Since the previous update, the following four (4) companies have come to trade: **B52 Investments Inc.**, **Emergence Resort Canada Inc.**, **Inter Energy Corp.** and **Rita Capital Corp.**

The following 13 companies have been removed from the list because they have completed their Qualifying Transactions making them regular listed companies: **Arbour Energy Inc.**, **Begama Technologies Inc.**, **Blueland Capital Inc.**, **Cross Border Capital Inc.**, **Crossroad Ventures Inc.**, **Cyan Corporation**, **Gateway Capital Corp.**, **Integrated Enviro-Capital Inc.**, **Marquette Capital Corp.**, **Smart Api Venture Capital Corporation**, **SVC Second Venture Capital Corp.**, **Typhoon Venture Capital Corporation**, and **Wrangler West Capital Corp.**

An introductory article explaining CPCs may be found at <http://www.bctechnology.com/statics/mvolker-jun0200.html>.

VEF Events

The **Vancouver Enterprise Forum** held a couple of weeks ago presented the ins and outs of taking a company public on the junior stock exchange - the TSX-Venture exchange. Two companies talked about their very positive experiences in raising capital using the CPC route.

One of these, **Carmanah Technologies Corp** (TSX-V:CMH, \$0.85) CEO and serial entrepreneur **David Green** noted that he had taken the Venture Capital route with his previous company - **NxtPhase Corporation**. This time around, he actually secured VC financing for Carmanah, but then had second thoughts and gave the money back to the VC's. He showed an interesting slide which may have explained why he did this. The slide showed (verbatim) some of the problems with venture capital as being: "warrants, ranking/rights on dissolution, dividends, retraction/redemption clauses, conversion rights, anti-dilution, preemptive rights, co-sale rights, tag-along rights, drag along rights, rights of first offer, right to sell in an IPO, remedies, demand rights, piggyback registrations, voting rights". He noted that with VC financing, you effectively lose control whereas with public investors, there are no large control blocks and the entrepreneur effectively retains control of the company.

In contrast, January's VEF topic was on Venture Capital financing and several companies presented their very positive experiences in dealing with VC's. It just shows that there's no one right way to raise money for a growing company. It all boils down to the chemistry and fit between the players. It's also nice to see that there are several options available to the technology entrepreneur.

Next month's VEF event scheduled for March 25th is titled, "Selling Strategies". Not much detail is available yet - so please check the VEF website soon.

A complete calendar of technology events can be found on [T-Net's Events page](#).

Footnotes

If you're an entrepreneur looking for a place to get your company started; there's some great

space available at Harbour Centre downtown. The **New Media Innovation Centre** (NewMIC) and **SFU's TIME Centre** have teamed up to provide not only office space but also access to various resources, e.g. tech advisors, access to capital, mentors, etc. Worried about the high cost of being downtown? Well, not to worry - they'll even reduce the fees and take some payment in the form of equity. Check www.sfu.ca/time for contact info.

A reminder: SFU's TIME Centre is open for business - business folks, that is. TIME is an acronym for **Technology, Innovation, Management, and Entrepreneurship**. TIME supports the growth and development of the tech industry in B.C. TIME features a "BusinessCentre" (looks like an airport business lounge) which is open to technology entrepreneurs and business people to use as a drop-in downtown office facility. Need to plug-in? Make some calls? Do some work? Hold a meeting? There are some great facilities for holding your company's AGM. Why hang out at MacDonald's when you can work productively at the TIMECentre? Drop by and check it out! It is located at SFU's downtown campus at 515 West Hastings St.

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