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WEBB & KNAPP (CANADA) LIMITED

ANNUAL REPORT 1977

HOWARD ROSS LIBRARY
OF MANAGEMENT
AUG 24 1979
McGILL UNIVERSITY

WEBB & KNAPP (CANADA) LIMITED

DIRECTORS

Edward R. Loftus
Charles B. Riley
Robert J. Dick

OFFICERS

Edward R. Loftus, President
Robert J. Dick, Vice-President, Treasurer
Margaret L. Munro, Secretary

TRANSFER AGENT AND REGISTRAR

Montreal Trust Company - Vancouver,
Toronto, Montreal, Winnipeg and Halifax

AUDITORS

Deloitte, Haskins & Sells
Chartered Accountants
Vancouver, B.C.

STOCK EXCHANGE LISTINGS

Vancouver and Montreal

HEAD OFFICE

400 Guinness Tower
1055 West Hastings Street
Vancouver 1, B.C.

REPORT TO SHAREHOLDERS

Your Directors are pleased to present herewith the Consolidated Financial Statements for the year ending December 31, 1977.

Your Company continues to expand the revenues of both the airline and rental income departments..

Although the revenues for Northern Thunderbird Air were up somewhat, they were far below management's expectations, particularly as a result of the termination of the B.C. Railway - Dease Lake construction program in April 1977. In spite of the fact that the closure of the Dease Lake railway extension substantially reduced revenues, the Company managed an overall increase in passengers carried by 20% over the previous year. The present capabilities of the airline are such that the Company will be in a strong position to service the interior of the Province of British Columbia at the time the economy improves. With constant management review, it is anticipated the profitability can be significantly increased without impairment of the long range aims of your Company.

The Board of Directors declared a dividend from the Surplus of the unconsolidated Company on the outstanding Preferred Shares, thereby reducing the dividends in arrears to what management considers an acceptable level.

During the year construction of warehouse space continued at Lake City Industrial Park and due to the excellent location of this development and our other industrial areas, the rental properties continue to prosper, and vacancy rates remain at a low level. As the economic problems of the Province do not have a material effect on this segment of your operations a continuing construction of buildings is anticipated.

Respectfully submitted,

E K Loftus

President

WEBB & KNAPP (CANADA) LIMITED

(Under the Canada Corporations Act)

AND SUBSIDIARY COMPANIES

CONSOLIDATED FINANCIAL STATEMENTS

AUDITORS' REPORT

To the Shareholders of
Webb & Knapp Canada Limited:

We have examined the consolidated balance sheet of Webb & Knapp (Canada) Limited as at December 31, 1977 and the consolidated statements of loss, deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the company as at December 31, 1977 and the results of its operations and the changes in financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, B.C.
May 5, 1978

DELOITTE, HASKINS & SELLS
Chartered Accountants

CONSOLIDATED BALANCE SHEET

AS AT DECEMBER 31, 1977
(with prior year's figures for comparison)

	1977	1976
ASSETS:		
Cash and term deposits	$ 32,076	$ 61,260
Accounts and notes receivable and other (Note 2)	367,612	1,284,637
Inventory of aircraft parts and fuel	145,271	187,438
Land held for future development (Note 3)	1,404,167	1,358,522
Revenue-producing properties (Note 4)	5,309,266	4,621,951
Aircraft (Note 4)	2,342,931	1,484,569
Other fixed assets (Note 4)	353,349	375,211
Deferred income taxes	33,372	41,830
Total assets	$9,988,044	$9,415,418
LIABILITIES:		
Bank loans (Note 5)	$ 864,327	$ 245,546
Accounts payable and accrued charges	543,772	264,846
Estimated income taxes payable (Note 6)	301,743	299,943
Long-term debt on (Notes 5 and 7):		
Revenue-producing properties	4,589,906	4,666,261
Aircraft	1,647,513	1,188,064
Undeveloped land	10,000	20,000
Advances from minority shareholder of subsidiary — no specific repayment terms	6,398	6,398
Deferred income	91,679	66,812
Total liabilities	8,055,338	6,757,870
MINORITY INTEREST IN SUBSIDIARY (represented by equity in preferred shares)	53,396	87,059
SHAREHOLDERS' EQUITY:		
Capital stock (Note 8):		
Preferred	1,000,000	1,000,000
Common	2,765,300	2,765,300
	3,765,300	3,765,300
Premium on issue of common shares	20,600	20,600
	3,785,900	3,785,900
Deficit	(1,906,590)	(1,215,411)
Net shareholders' equity	1,879,310	2,570,489
TOTAL	$9,988,044	$9,415,418

Approved by the Board:

EDWARD R. LOFTUS, Director

CHARLES B. RILEY, Director

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENT OF DEFICIT

FOR THE YEAR ENDED DECEMBER 31, 1977
(with prior year's figures for comparison)

	1977	1976
BALANCE AT BEGINNING OF THE YEAR	$1,215,411	$2,172,576
NET LOSS (INCOME) FOR THE YEAR	91,179	(957,165)
	1,306,590	1,215,411
DIVIDEND PAID ON PREFERRED SHARES	600,000	—
BALANCE AT END OF THE YEAR	$1,906,590	$1,215,411

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

FOR THE YEAR ENDED DECEMBER 31, 1977
(with prior year's figures for comparison)

	1977	1976
SOURCE OF FUNDS:		
From operations — representing net income or loss after adjusting for charges and credits for depreciation, deferred income taxes, unearned income and minority interest which do not involve a flow of funds	$ 178,901	$ 227,279
From extraordinary income	3,097	—
Increase in bank loans:		
Construction	270,000	—
Operating	348,781	—
Increase in accounts payable and accrued charges	278,926	—
Increase in estimated income taxes payable	1,800	30,500
Increase in long-term debt for aircraft	832,000	—
Increase in deferred income	30,000	—
Decrease in mortgage receivable	950,000	—
Decrease in inventory of aircraft parts and fuel	42,167	—
Proceeds from sale of undeveloped land (net of $950,000 mortgage receivable in 1976)	—	392,871
Insurance and sale proceeds on aircraft	905,780	70,800
Decrease in cash	29,184	—
	$3,870,636	$ 721,450
USE OF FUNDS:		
Increase in accounts and notes receivable and other	$ 32,975	$ 41,249
Increase in inventory of aircraft parts and fuel	—	63,164
Additions to land held for future development	78,214	65,052
Additions to:		
Revenue-producing properties	778,159	66,432
Aircraft (including expenditures on engine overhaul)	1,906,082	116,662
Other fixed assets	16,300	32,232
Reduction in operating bank loans	—	9,454
Decrease in accounts payable and accrued charges	—	53,841
Repayment of long-term debt	458,906	230,300
Dividend paid on preferred shares	600,000	—
Increase in cash	—	43,064
	$3,870,636	$ 721,450

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENT OF LOSS

FOR THE YEAR ENDED DECEMBER 31, 1977
(with prior year's figures for comparison)

	1977	1976
REVENUE		
Rental income	$1,021,784	$ 945,697
Airline revenues	1,999,853	1,917,042
Interest on agreements for sale and other	24,180	18,142
	3,045,817	2,880,881
COSTS AND EXPENSES:		
Direct operating before the undernoted:		
Rental operations	189,093	156,108
Airline operations	1,259,821	1,091,439
General and administrative:		
Rental operations	283,522	307,681
Airline operations	503,396	446,974
Interest on long-term debt:		
Rental operations	466,847	473,214
Airline operations	155,207	144,911
Depreciation and amortization:		
Rental operations	134,867	129,784
Airline operations (including provision for engine overhaul)	334,751	298,175
Loss on aircraft disposals	32,520	—
Interest on income tax reassessments and unpaid income taxes	10,397	13,668
	3,370,421	3,061,954
LOSS BEFORE THE UNDERNOTED	324,604	181,073
(RECOVERY OF) PROVISION FOR INCOME TAXES:		
Current	(6,500)	9,485
Deferred	(54,904)	(79,550)
	(61,404)	(70,065)
LOSS BEFORE MINORITY INTEREST AND EXTRAORDINARY INCOME	263,200	111,008
MINORITY INTEREST'S SHARE OF OPERATING LOSS OF A SUBSIDIARY	72,889	13,504
LOSS BEFORE EXTRAORDINARY INCOME	190,311	97,504
EXTRAORDINARY INCOME (Note 9)	99,132	1,054,669
NET LOSS (INCOME) FOR THE YEAR	$ 91,179	$ (957,165)
LOSS (INCOME) PER COMMON SHARE (Note 10):		
Loss before extraordinary income	$ .09	$ .05
Net loss (income) for the year	$ .05	$ (.33)

The accompanying notes are an integral part of the consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1977

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Principles of consolidation:

The consolidated financial statements include the accounts of the company and all of its subsidiaries, all of which are wholly-owned except for Northern Thunderbird Air (N.T. Air), of which the company owns 66% of the issued common shares and 71% of the issued preferred shares.

Inventory of aircraft parts and fuel:

The inventory of aircraft parts and fuel is valued principally at first-in, first-out cost.

Land held for future development:

Land is recorded at its original cost plus property taxes ($105,300 and $102,902 in property taxes were capitalized in 1977 and 1976 respectively).

Revenue-producing properties:

All interim financing charges and the cost of supervisors' salaries incurred up to the date of structural completion of a project are capitalized as part of the cost of buildings ($27,726 and $nil were capitalized in 1977 and 1976 respectively).

Aircraft:

Used aircraft acquired which have a lapsed engine life are capitalized at original cost plus an estimate of the cost of engine overhaul.

Depreciation, amortization and provision for engine overhaul:

Depreciation and amortization are provided principally on a straight-line basis at the rates shown in Note 4, except for construction in progress, where no depreciation is provided until occupancy reaches the 50% level.

The Ministry of Transport regulations require that aircraft engines be overhauled within prescribed flying limits. A provision is made based on an estimated cost per hour. The accumulated allowance is accounted for as a reduction of the carrying value of the aircraft.

Deferred income:

Deferred income, which consists principally of prepaid rentals, is being credited to income on a straight-line basis over the terms of the leases.

2. ACCOUNTS AND NOTES RECEIVABLE AND OTHER:

	1977	1976
Accounts and notes receivable:		
Trade	$ 335,825	$ 264,716
Officers and directors	17,122	12,139
	352,947	276,855
Mortgages and notes receivable	13,393	956,318
Deposit on purchase of aircraft	—	50,000
Prepaid expenses and deposits	1,272	1,464
	$ 367,612	$1,284,637

3. RAILWAY LEAD TRACK:

Included in the balance sheet caption, land held for future development, is an amount of $182,742, representing construction costs of $340,672 for a railway lead track which are recoverable from a railway company, less refundable amounts of $157,930. The costs are recoverable at a rate based on usage of the track.

Repayment of the refundable amounts shall commence once such amounts equal the balance of the recoverable costs and at a rate based on the greater of future usage of the track or the rate at which the funds were loaned to a subsidiary. This amount is non-interest-bearing.

4. REVENUE-PRODUCING PROPERTIES, AIRCRAFT, AND OTHER FIXED ASSETS:

	Depreciation and Amortization Rates	1977	1976
Revenue-producing properties:			
Land		$ 362,158	$ 323,518
Buildings (including construction in progress of $589,160 in 1977 and $67,092 in 1976)	2½%	5,482,795	4,710,708
Total cost		5,844,953	5,034,226
Less accumulated depreciation		535,687	412,275
		5,309,266	4,621,951
Aircraft and related equipment:			
Total cost	10% of 80% of cost	2,872,093	1,859,327
Less accumulated depreciation and allowance for engine overhaul		529,162	374,758
		2,342,931	1,484,569
Other fixed assets:			
Land	—	44,000	44,000
Buildings	4%-10%	217,149	214,962
Ground radio equipment	20%-25%	63,270	60,519
Automotive equipment and trailers	10%-30%	64,189	61,399
Office and shop equipment	20%	37,363	36,923
Furniture and fixtures	20%	36,883	35,347
Railway lead track	6%	103,988	103,988
Leasehold improvements	20%	11,733	11,733
Total cost		578,575	568,871
Less accumulated depreciation and amortization		225,226	193,660
		353,349	375,211
		$8,005,546	$6,481,731

5. PLEDGED ASSETS

(a) The company and certain of its subsidiaries have made a general assignment of book debts as security for outstanding operating bank loans of $594,327.
In addition, a subsidiary has issued a debenture with a second floating charge on all of its other assets.

(b) As security for its construction bank loan of $270,000, a subsidiary has furnished the bank with a certificate of title to a revenue-producing property with a carrying value of $671,728.

(c) Long-term debt (Note 7) is secured by:

	Carrying Value of Assets at December 31, 1977
Mortgages on revenue-producing properties — charges against respective revenue-producing properties	$4,608,857
Mortgages and loans on aircraft — mortgage on certain owned and leased properties, debentures and chattel mortgages with a first fixed and second floating charge on aircraft and certain other assets	$2,753,099
Agreement payable — title to related property	$ 54,718

Certain subsidiaries have assigned, or have agreed to assign, the leases on certain revenue-producing properties as additional collateral for the mortgages payable.

6. INCOME TAXES:

During 1976 the Tax Review Board dismissed the appeal of notices of reassessment issued in 1975 by the Department of National Revenue, Taxation to certain active subsidiaries in respect of their 1971 and certain other prior taxation years. On February 11, 1977 the subsidiaries filed Notices of Appeal with the Federal Court, which have not yet been heard.

The subsidiaries have, however, provided for the estimated income tax liabilities resulting from these reassessments together with interest thereon.

The liability at December 31, 1977 includes $283,186 representing a subsidiary's unpaid balance of 1972 income taxes, including interest accrued thereon to December 31, 1977. This amount has not been paid pending the appeal referred to above.

Because of losses incurred by N.T. Air prior to acquisition, no recognition has been given in the accounts to a deferred income tax debit (representing a future potential income tax savings) relative to the excess of depreciation and provision for engine overhaul recorded in the accounts over the related amounts claimed for income tax purposes, which excess amounts to approximatey $339,000 at December 31, 1977. Also, no recognition has been given in the accounts to a future potential income tax saving relative to this subsidiary's tax loss carry-forward of $44,000 as at December 31, 1977, which expires in 1982.

7. LONG-TERM DEBT:

	Maturing in	1977	1976
Mortgages on revenue-producing properties:			
9.0%	1993	$ 225,217	$ 231,663
9.5%	1995	369,472	377,984
9.5%	1999	2,065,912	2,093,967
10.5%	1996	385,181	391,962
11.0%	1990	1,544,124	1,570,685
		4,589,906	4,666,261
Mortgages and loans on aircraft:			
10.1%	1981	393,557	485,330
Prime bank rate (8.25% at December 31, 1977):			
Plus 1.75%	1981	242,211	432,721
Plus 2.0%	1984	781,655	—
Plus 2.5%	1982	230,090	270,013
		1,647,513	1,188,064
Agreement payable on undeveloped land:			
8.0%	1978	10,000	20,000
		$6,247,419	$5,874,325

In connection with one of the 9.5% mortgages and the 10.5% mortgage, a subsidiary is required to pay certain percentages of gross annual income with minimum aggregate payments of $2,120 ($10,472 and $7,663 were payable for 1977 and 1976).

The aggregate principal payments due in the next five years on long-term debt approximate:

1978	—	$396,000	1981	—	$381,000
1979	—	430,000	1982	—	299,000
1980	—	477,000			

8. CAPITAL STOCK:

The authorized and outstanding capital stock of the company is as follows:

	1977	1976
Authorized:		
2,000,000 redeemable preferred shares of a par value of $5 each, issuable in one or more series		
10,000,000 common shares of a par value of $1 each		
Issued and fully paid:		
200,000 5% cumulative voting preferred shares, Series A, redeemable at 105% of the par value	$1,000,000	$1,000,000
2,765,300 common shares	2,765,300	2,765,300
	$3,765,300	$3,765,300

As at December 31, 1977, the arrears of dividends on the outstanding preferred shares amounted to $50,000 (1976 - $600,000).

9. EXTRAORDINARY INCOME:

Extraordinary income consists of the following:

	1977	1976
Wholly-owned subsidiaries:		
Gains on sale of land (net of current income taxes of $17,554 and deferred income taxes of $228,179)	$ —	$1,039,527
Realization of tax saving on applications of loss carry-forwards	3,097	—
	3,097	1,039,527
Partially-owned subsidiary:		
Excess of insurance proceeds over net book value of aircraft (net of deferred income taxes of $63,364 in 1977 and $17,000 in 1976)	135,261	21,327
Less minority interest's share thereof	39,226	6,185
	96,035	15,142
	$ 99,132	$1,054,669

10. LOSS (INCOME) PER COMMON SHARE:

The net loss (income) per common share has been calculated in accordance with the dividend priorities attached to each class of share. Accordingly, the loss (income) for the current and preceding years reported in the accompanying consolidated statement of loss has been adjusted by $50,000, being the annual arrears of cumulative dividends on the outstanding preferred shares.

11. LEASE COMMITMENTS AND OPTIONS:

Commitments under long-term leases require the following approximate minimum annual payments:

Leases on revenue-producing properties:

1978	—	$108,500
1979	—	48,500
1980	—	43,500
1981	—	25,000
1982 to 1999	—	19,000

Lease on office and other premises:

1978 to 1979	—	$ 36,000
1980	—	27,500
1981	—	15,500

Certain of the lease agreements contain renewal provisions for additional three-to-five year periods at rentals to be negotiated. One of the leases on revenue-producing properties also provides for the payment of 50% of the annual rentals (as defined) received in excess of $63,510 annually ($18,288 and $12,648 were payable for 1977 and 1976 respectively).

A subsidiary has options to lease certain other premises in 1982 through to 1984 for periods up to ten years at aggregate annual rentals of $25,000. These option agreements provide that the subsidiary may sublet the premises and retain any rentals received in excess of the required rental payments.

12. OTHER CONTINGENT LIABILITIES:

(a) The company has guaranteed or is contingently liable for the performance of various obligations of another corporation of which the company was formerly a major shareholder. Consequent upon the sale in 1964 of the company's investment in the other corporation, that corporation and certain of its other major shareholders have agreed to indemnify the company against any such liability.

(b) There are certain claims in unspecified amounts pending against the airline subsidiary. Management is of the opinion that any liability arising from these claims will be adequately covered by its insurance policy.

(c) In 1973, an inactive subsidiary, which had no assets according to its December 31, 1971 audited financial statements, received notices of reassessment from the Department for the taxation years 1963 to 1969 inclusive whereby its reported taxable incomes were increased. Management disagrees with these reassessments and accordingly, no provision has been made in the accounts for a possible liability of approximately $105,700 (exclusive of interest thereon) for that company's 1969 taxation year.

13. SUBSEQUENT EVENT:

Subsequent to December 31, 1977 a subsidiary negotiated a mortgage of $775,000 to finance construction of a revenue-producing property. This mortgage will bear interest at 10½%, and will be repayable in monthly amounts of $7,626 for principal and interest. The full advance will be received upon substantial completion of construction and the signing of sufficient leases for the property to meet a level of rental income required by the agreement. The proceeds will, in part, be used to repay the outstanding construction bank loan (Note 5(b)).

14. REMUNERATION OF DIRECTORS AND OFFICERS:

The total remuneration of directors and officers, as defined in the Canada Corporations Act, for the year was as follows:

The company's three directors received no remuneration as directors of the company or its subsidiary companies.

The company's three officers received no remuneration as officers of the company.

The company's three officers received $85,868 as officers of a subsidiary company.

Two of the company's officers are also directors.

15. ANTI-INFLATION LEGISLATION:

The company is subject to the provisions of the Anti-Inflation Act, which restricts the payment of dividends during the twelve-month period ending October 13, 1978. Because of the arrears of dividends on preferred shares (Note 8), the payment of which is not restricted by legislation, it is expected that the Act will not affect the company.

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