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***Delta Fur Company Limited - Audit Report
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DELTA FUR COMPANY LIMITED - AUDIT
REPORT

Sector: Wildlife Products

5-6-80

Analysis/Review

DEC - 5 1984

Audit Report

DELTA FUR COMPANY LIMITED

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DELTA FUR COMPANY L.IMITED



File: 61-05-22-105

July 11, 1984

COMMISSIONER

Audit Report: Department of Economic Development and Tourism
Delta Fur Company Limited
Audit Period: April 1, 1980-- January 31, 1984

A. SCOPE

We have conducted an audit of Delta Fur Company Limited (Delta Fur) by special request of the Department of Economic Development and Tourism (Department). This review included a detailed examination of the company's financial records since April 1, 1982, in order to prepare current financial statements; furthermore, we reviewed all available internal government and company files concerning Delta Fur since its inception. We have performed such tests, analyses and other procedures as we considered necessary in the circumstances, except as noted below.

Internal controls underlying the accounting system and financial records of the company could not be tested adequately. Most government and company employees who had been associated with Delta Fur were no longer available. Furthermore, the existing records and information pertaining to Delta Fur were neither complete nor in good order.

B. EXECUTIVE SUMMARY

1. Background

Upon the direction of the Department, Delta Fur was incorporated on October 9, 1979, under the Canada Business Corporations Act (C.B.C.A.). The main purpose for this action was to merge the Aklavik and Tuktoyaktuk Fur Garment Co-operatives, "in order to revitalize and rationalize the Tuk and Aklavik Fur Shop operations". Furthermore, the studies which led to the recommended incorporation of Delta Fur were "to determine whether the shops could be operated with the requirement that any government subsidies necessary would not exceed the value of the wage bill."

Prior to Delta Fur's incorporation, the government had managed the two Fur Garment Co-operatives on an interim basis until April 1, 1980.

The government provided Delta Fur with an opening inventory valued at \$212,000, a cash Contribution of \$125,000 and a revolving fur fund of \$600,000. In addition, Delta Fur was provided with the use of government buildings and production equipment at no charge,

Severe financial difficulties finally forced the company to cease operations on December 23, 1982.

2. a) Report Introduction

Audit observations are presented in section C of this

report; also, recommendations for corrective action or improved results during any future endeavors of this nature are offered wherever practical. All schedule references refer to the schedules which are included in Appendix A. Appendix B contains information which may be of use to the Department with respect to several matters that are still outstanding.

All observations were discussed with headquarters and regional Department staff at the conclusion of our audit. A final review of the draft report was held on June 13, 1984, with the Assistant Deputy Minister of the Department and the Comptroller General. Department management has indicated that it does not wish to provide written responses for inclusion in the report at this time.

b) overview

Delta Fur ceased operations on December 23, 1982, and is financially insolvent. In addition, the government's investment, estimated to be over \$938,000, greatly exceeded the local wages (\$483,000) that were paid by Delta Fur. Accordingly, the Department's apparent objectives were not realized. The reorganization of the Aklavik and the Tuk Fur Garment Co-operatives into Delta Fur on April 1, 1980, did not "revitalize and rationalize" these operations as envisioned by the Department.

Delta Fur has never been consummated as a company in all legal and organizational respects. Consequently, a tangle of legal questions remain to be resolved.

Delta Fur commenced operations at the direction of the Department before full-time company management was in place. In fact, the Department never was successful in recruiting a permanent management team. Instead, government employees acted in the capacity of president to enable the company to begin and maintain operations as had been promised by the Department.

Company operations continued even after the company's main customer, Arctic Marketing Enterprises, ceased to function in November, 1980. Sales thereafter plummeted from \$647,000 in 1980-81 to \$173,000 in 1981-82, an event that should have led to serious questions with respect to Delta Fur's future as a going concern.

Moreover, despite the sales decline, large purchases were added to the Revolving Fur Fund inventory in 1982.

There was ample evidence that Delta Fur should have closed operations in 1981. Even before Delta Fur commenced operations, the Inuvik Regional Director, on March 20, 1980, pointed out, to the Director, Regional Operations and the Deputy Minister of the Department, deficiencies that were sufficiently serious to warrant discontinuation of the undertaking.

In our opinion, the Department acted in haste to begin Delta Fur operations, and did not discharge its continuing responsibilities after bringing the company into existence without full-time management. Furthermore, the Department did not make the hard decision to recommend Delta Fur's closure when, by 1981, the economic evidence was conclusive.

C. OBSERVATIONS AND RECOMMENDATIONS

1. Current Financial Position

Observation

- a) In conjunction with this audit, we have prepared the following balance sheet as at January 31, 1984, as well as a statement of profit and loss for the ten months then ended.

These statements were prepared from incomplete financial information because not all of the source documents, journal entries and other supporting records were available to us. The condition of those records that were available was very poor. Moreover, the reliability of control over sales and cash receipts was doubtful. Therefore, we caution the reader that we cannot provide assurance regarding the accuracy of the amounts presented in the balance sheet and statement of profit and loss.

- b) The financial position of the company as at January 31, 1984, is reflected in the balance sheet. Current liabilities exceed current assets by approximately \$11,000 and there is enough cash to cover only one-half the amount owing to creditors. Furthermore, net realizable value of the inventory and fixed assets would probably be substantially lower than the book value reported on the balance sheet. Therefore, Delta Far is financially insolvent.

The statement of profit and loss for the period from April 1, 1982, to January 31, 1984, discloses a net loss of \$113,876. Actual production in this period was 408

nine months only (April, 1982, to December, 1982) because Delta Fur operations were shut down on December 23, 1982.

The gross margin loss of \$78,448 **is** the most significant fact that the statement of profit and loss reveals. This loss was due to the fact that the cost of goods sold (\$307,292) was substantially higher than the revenue realized by the sale of the goods (\$228,246).

DELTA FUR COMPANY LIMITED
BALANCE SHEET
AS AT JANUARY 31, 1984

ASSETS

Current

Cash	\$40,612
Accounts receivable (Schedule A)	65,214
Less: Allowance for doubtful accounts	(48,910)
Employee advances	2,500
Inventory (Note 1)	<u>12,249</u>
	71,665

Fixed

Patterns	5,000
Accumulated depreciation	(1,500)
Office equipment	1,059
Accumulated depreciation	<u>(635)</u>

TOTAL ASSETS

\$75,589

LIABILITIES

Current

Bank overdraft (Note 2)	\$ 297
Accounts payable (Schedule B)	9,060
Payroll taxes payable	294
G.N.W.T. revolving fund payable	<u>73,117</u>

TOTAL LIABILITIES

82,768

SHAREHOLDERS' EQUITY

Contributed surplus (Note 3)	337,153
Share capital	2
Deficit	<u>(344,334)</u>
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u><u>\$ 75,589</u></u>

DELTA FUR COMPANY LIMITED
STATEMENT OF PROFIT AND LOSS
FOR THE PERIOD APRIL 1, 1982 TO JANUARY 31, 1984

REVENUE:

Sales	\$228,246
Cost of goods sold	<u>307,292</u>
Gross margin	<u>19,046</u>)
Miscellaneous revenue	598

(78,448)

OVERHEAD EXPENSES:

Administrative salaries	15,834
Rent & utilities	11,785
Travel	1,472
Interest & bank charges	1,934
Professional fees	1,034
Office	1,392
Communications	1,435
Insurance	93
Advertising	
Repairs & maintenance	
Depreciation & amortization	1,424
Miscellaneous expense	<u>1,186</u>

Operating loss (116,037)

Interest on term deposits 2,161

Net loss \$(113,876)

NOTES

(1) Inventory was taken February 2, 1984, and valued at cost.

(2) Bank overdraft (C.I.B.C.) was paid in February, 1984.

(3) Opening inventory (\$212,153) and Assistance to Industry contribution (\$125,000) were advanced to Delta Fur by the GNWT . The inventory was advanced in consideration for an issue of preferred class 'B' shares. These shares were never issued.

2. Legal Status of Company

Observation

Delta Fur ceased operations on December 23, 1982, is financially insolvent, and is probably in a state of dissolution according to the C.B.C.A. under which it is registered.

The company may have defaulted under the fur revolving fund loan agreement and the debenture made by the company with the Commissioner, both dated June 9, 1980. Terms of the agreements in the event of default allow the Commissioner to appoint a receiver and sell Delta Fur's assets in order to satisfy the outstanding debt owing to the government. Ordinarily, when revolving fund Issue Vouchers 28295, 28296 and 28298, dated in November and December of 1981, became payable in May, 1982, and were not paid by the company, the terms of the agreements would have become enforceable. The remedies allowed the government under these agreements in the event of default were never exercised by the Department.

However, there is a legal deficiency as the government neglected to enforce the requirement for promissory notes "to evidence" revolving fund fur issues according to the loan and debenture agreements.

Delta Fur is also vulnerable to dissolution procedures under sections 205 and 206 of the C.B.C.A. Under section 205, the Director of the Act may dissolve the company if it "is in default for a period of one year in sending the Director any fee, notice or document required by this Act". Delta Fur has not submitted the annual return required by section 256 since 1981. In addition, section 206 may be invoked by the director as he has grounds for

dissolution because Delta Fur had "failed for two or more consecutive years to comply with the requirements of this Act with respect to holding of annual meetings of shareholders". The last general meeting of shareholders on record was held on July 15, 1981.

We conducted a search of the documents registered with the C.B.C.A. and found that the only directors on record were the corporate lawyer and his secretary.

As mentioned in observation one, Delta Fur is financially insolvent. As a result, operations ceased on December 23, 1982, and the company has no reasonable financial prospects to re-open.

The lawyer who has acted for Delta Fur advised us that he considered Delta Fur's legal file to be dead. The lawyer's requests for current lists of the company's directors on March 25, 1982, addressed to the Chairman of the Finance Committee, remain unanswered.

The company lawyer advised us that the best course of action, in light of Delta Fur's present financial and legal position, would be to have the board of directors dissolve the company and appoint a receiver to properly wind up its affairs. Legal costs to prepare and process the company's dissolution would be an estimated \$600.

Recommendation

We recommend that the Department give consideration to obtaining legal counsel and winding up the company.

3. Capital and Organizational Structure

Observation

The capital and organizational structure of Delta Fur was unnecessarily elaborate and deficient (Schedules C and D refer).

a. Share Structure

There were three classes of common shares and two classes of preferred shares.

Class 'A' and class 'B' common shares were to be held by two "holding companies" incorporated in the N.W.T. The holding companies would each be owned by the respective Delta Fur employees in Aklavik and Tuktoyaktuk.

Class 'A' preferred shares were to be issued as non-cash performance dividends on 'A' and 'B' common shares. Class 'B' preferred shares were to be exchanged as collateral for the \$212,000 in inventory that was provided by the government.

Class 'C' common shares were to be issued upon the conversion of preferred 'B' shares in the event of Delta Fur's insolvency or inability to operate. Class 'C' common shares would then provide the government with controlling interest in Delta Fur.

The net result of this complex share structure was to confuse the worker-owners as to the tangible stake they had in Delta Fur. A worker-owner was removed from Delta Fur by two corporate levels in addition to management under this structure. The additions of C.O.P.E. , I.D.C. and the G.N.W.'l'. as directors of Delta Fur complicated matters further.

b. Organizational Structure

The approved organizational structure for Delta Fur established the company president as senior executive officer. The president was accountable to an **eight-** member board of directors.

The structure also provided for a five-member finance committee, chaired by an employee of the **GNWT**. Although nominally a sub-committee of the board, the finance committee, vested by the company's by-laws with broad powers of veto over board decisions in borrowing, banking, legal execution of documents, audits and budgets, and acting in an influential manner throughout the period of **Delta Fur's** existence as an active company, exercised de facto control over the affairs of the company.

Delta Fur's organizational structure required the company's accountant (Secretary/Treasurer) to report directly to the finance committee chaired, as previously mentioned, by a Department employee. This type of relationship circumvented the company's president, who had only the Aklavik and Tuktoyaktuk plant managers reporting to him, and resulted in an untenable reporting/accountability process.

4. Regional vs Headquarters Responsibilities

Observation

(a) The Department of Economic Development and Tourism, headquarters was responsible for the planning and implementation of Delta Fur.

Headquarters commissioned numerous studies on the Aklavik and Tuktoyaktuk fur shops which recommended the implementation of Delta Fur. Headquarters also initiated the following actions:

- i) submitted recommendations for Delta Fur to the Executive Committee for approval;
- ii) requested funding for the company;
- iii) obtained the necessary legal advice with respect to the incorporation of Delta Fur;
- iv) hired consultants to recruit Delta Fur management and recruited management directly;
- v) hired a Secretary, "Treasurer for the company;
- vi) nominated a headquarters employee to act as finance committee chairman;
- vii) recommended the establishment of a revolving fund.

- (b) The Inuvik Regional Director outlined his concerns about the lack of regional participation and the future prospects of Delta Fur in a memorandum dated March 20, 1980. In hindsight, these concerns were well founded. Due to the unsuccessful efforts by the Department to recruit a president from the private sector, the Regional Superintendent was approached by headquarters to fill this job during 1980. Subsequently, the position of president was usually staffed by the Regional Superintendent.

A formal transfer of responsibility from headquarters to the region did not occur, yet, the headquarters employee who acted as the chairman of Delta Fur's finance committee told us on several occasions during the audit that he no longer had anything to do with Delta Fur. The regional office continued to exercise day to day operational responsibilities but felt they could not act beyond this scope. Therefore, despite the fact that the Regional Superintendent of Economic Development acted as the President of Delta Fur, it would appear that the headquarters' staff of the Department, by its actions, retained responsibility for the company.

Recommendation

We recommend that, at such time as the Department enters any major undertaking such as Delta Fur, a memorandum be drafted outlining the respective responsibilities of headquarters and regional offices. This memorandum should be amended whenever changes to the responsibilities occur.

5. Opening Inventory

Observation

The government transfer of \$212,000 in inventory to Delta Fur, on March 26, 1980, was never secured by class 'B' preferred shares as approved by the Executive Committee's Record of Recommendation 80-11-4. In an exchange of memorandums dated December 19, 1980, the Comptroller General stated that the government may not hold Delta Fur preferred shares as they do not meet the financial criteria established under the Financial Administration Ordinance. We could find no evidence of subsequent action by the Department to deal with the issue of the opening inventory. Therefore, because the class 'B' preferred shares were not issued, and no agreeable alternatives **were** implemented, this issue remains unresolved. The matter must, of course, be resolved in the event of the dissolution of Delta Fur.

Recommendation

We recommend that the appropriate accounting treatment, and, if necessary, write-off action, with respect to the opening inventory, be effected by the Department.

6. Marketing

Observation

(a) The drastic decline in sales that occurred subsequent to November, 1980, was the major financial cause of the failure of Delta Fur.

Between April and November, 1980, an estimated seventy-five percent of Delta Fur's production had been sold to Arctic Marketing Enterprises, a government agency within the Department that had been established to purchase and distribute northern products. Arctic Marketing Enterprises ceased operations in November, 1980; from that point on, Delta Fur's sales declined rapidly and never recovered (Schedules E, F & G refer), and the Department was no longer able to provide effective marketing assistance.

The following table illustrates the severity of the sales decline:

<u>Fiscal Year</u>	<u>Total Annual Sales</u>	<u>Average Monthly Sales</u>	<u>Percentage Increase/Decrease From Prior Period</u>
1980/81	\$647,000	\$54,000	
1981/82	\$173,000	\$14,000	(275%)
1982/83	\$228,000	\$19,000	<u>36%</u>
Net decline			<u>(239%)</u>

(Note - Annual sales amounts for 1980-81 and 1981-82 were extracted from financial statements. These amounts do not agree to the sales amounts per the company's sales journals, which were the source of the information presented in Schedule E. 1982-83 sales were calculated during our audit).

The root of the marketing problem can be traced back to the sales forecasts that were presented to the Executive Committee on March 21, 1980:

<u>Fiscal Year</u>	<u>Annual Sales Forecast</u>
1980/81	\$ 975,000
1981/82	\$1,341,000
1982/83	\$1,449,000

These forecasts were developed notwithstanding that Delta Fur had no means by which it could vigorously pursue independent distribution of its product, as well as the fact that the past sales history of the Aklavik and Tuktoyaktuk Fur Co-ops, Delta Fur's predecessors, for the fiscal years 1977 and 1978, indicated actual monthly sales of \$35,000. Achievement of the forecasted sales as presented above would have required the following annual increases, in percentage terms, in comparison with the actual sales experience of the co-ops:

<u>Fiscal Year</u>	<u>Average Monthly Sales</u>	<u>Percentage Increase Over Previous Period</u>
Co-ops actual 1977/78	\$ 35,000	
Delta forecast 1980/81	\$ 81,000	131%
Delta forecast 1981/82	>112,000	38%
Delta forecast 1982/83	\$121,000	<u>8%</u>
Total sales increase		<u>177%</u>

(Note: Actual sales amounts for 1978-79 and 1979-80 were not available).

These optimistic sales increases were projected in spite of actual history to the contrary and without a comprehensive sales plan to support the reasonableness of the projections. This left unanswered the question as to how these sales were to be achieved.

- (b) In July, 1982, Northern Images evidently offered to purchase up to **999** parkas annually from Delta Fur. This offer represented over one hundred percent of Delta Fur's foreseeable production, yet, despite the sales decrease being experienced, the offer was apparently rejected.

In addition to the sales volume problem, Delta Fur was experiencing quality control problems with its products. For example, one bulk purchase by Northern Images of 223 parkas included 40 which had seam splits, as well as sleeve lengths that were shorter than had been specified in the patterns.

7. Revolving Fund

Observation

The Delta Fur revolving fund was not managed in a prudent manner, which increased government exposure to large losses.

Despite the marked **sales** decline that had been experienced by Delta Fur after November, 1980, large additional raw fur purchases were made by the Department (Schedule H refers). In March, 1981, the balance of the revolving fund inventory was \$328,000, yet, fur purchases during the year increased the balance to a high of \$388,000. **The last issues to Delta Fur in 1981** amounted to \$74,000 thus reducing the revolving fund fur inventory to \$314,000 until February, 1982. Then, in February and March, 1982, over \$105,000 in purchases were made when in fact there was an urgent requirement to reduce the inventory. By February, 1982, Delta Fur sales were known to have declined from \$647,000 in 1981 to **about \$170,000** for a twelve month period. Serious doubts concerning Delta Fur's survival should have existed by this time; accordingly, it is virtually inconceivable that prudent management would allow major inventory additions to take place.

By October, **1982**, the revolving fund fur inventory balance had increased to \$442,000. No furs were issued from the revolving fund inventory to Delta Fur in **1982** and, on January 25, 1983, the Comptroller General issued a telex directing that no further issues be made.

Furthermore, fur inventory is a commodity type inventory that is subject to wide market price fluctuation and physical deterioration. Unfortunately, the fur market experienced a deep decline after 1982 which, combined with

the effects of physical deterioration, resulted in the fur inventory having a book value that was higher than market value by approximately \$172,000 as of June, 1983.

Fur issues to Delta Fur were to have been evidenced by promissory notes according to the loan and debenture agreements dated June 9, 1980. Promissory notes were never used for fur issues, including the last issues which remained unpaid. Legal problems are now being faced by the government **because of the fact that** promissory notes were not obtained.

We have sought legal opinion as to whether or not the fur in the revolving fund could be sold to any party other than Delta Fur. To date, we have had no response to the request for this opinion.

Recommendation

We recommend that the Department obtain legal opinion as to whether or not the revolving fund inventory can be sold to any party other than Delta Fur. If the fur can be sold in this manner, then, we further recommend that it be disposed of and that any losses arising from the sale be submitted for write-off. In the event that the fur cannot be sold to a Party other than Delta Fur, legal action to correct this condition should be considered.

8. Government Employees as Board Members and Acting Presidents

Observation

The departmental submission to the Executive Committee regarding Delta Fur had specified a full time manager in the position of president. When operations commenced on April 1, 1980, a GNWT employee was acting as president. Shortly after, that government employee was replaced by another, also in an acting capacity. With two exceptions, both for insignificant amounts of time, various government employees acted as president of the company throughout the lifespan of its operations.

Inasmuch as the company never had a full time president for more than a month, the daily affairs of the company were, on many occasions, left to local employees, the finance committee, or the board. This arrangement was awkward and unworkable for a private enterprise that required frequent executive decisions which could not wait for committee approval.

The Department also placed two employees on the company's board of directors in order to safeguard government interests. These positions changed hands on several occasions, yet there was no evidence that employee resignations from the board had been sanctioned by senior managers of the Department.

For example:

<u>Name</u>	<u>Date Appointed</u>	<u>Date Terminated</u>
Reaburn, B.	March 13, 1980	? 1982
Patterson, D.	March 13, 1980 June 30, 1980	June 17, 1980 July 15, 1981

Nigh, P.	June 17, 1980	November 12, 1980
O'Neill, D.	November 17, 1982	

The Departments of Economic Development and Personnel have confirmed that no policies exist with respect to employee participation as directors of external organizations on behalf of the government.

Recommendation

We recommend that the Department initiate the development of a policy for circumstances where it is considered to be desirable to have employees act as directors of external entities, as well as procedures regarding appointment to and resignation from such boards.

9. Finance Committee

Observation

The finance committee and, more specifically, the chairman, did not perform their duties adequately.

Delta Fur by-laws required the finance committee to supervise all bookkeeping and accounting functions including the preparation of budgets.

The 1981 financial statements, which were tabled at the July 15, 1981, **annual** meeting, contained a complete disclaimer by the company's auditors, Adams, Mann, Hinchey and Co., due to the lack of internal control. Evidence noted during our examination of Delta Fur's records disclosed that internal control remained unsatisfactory, and, after January, 1983, became unacceptable.

For example:

- a) there was no accountable forms control on invoices and cheques;
- b) the synoptic journals (books of original entry), since June, 1982, contained unaccountable entries, and the journals would not balance in every instance;
- c) bank reconciliations since June, 1982, were missing;
- d) the payroll imprest account was not used properly, as the bank transfers into the account did not reflect the actual payroll amount required;

- e) payments for expenses were issued from cash receipts instead of through the company's general bank account;
- f) after January, 1983, the synoptic journal was no longer maintained;
- g) payments made to creditors after January, 1983, were made mainly by bank drafts, and authorized only by the Area Economic Development Officer, instead of by company cheque and proper signing authorities;
- h) Delta Fur's files and records were generally in poor condition.

Furthermore, the company's by-laws, and the Canada Business Corporations Act, require the annual appointment of an auditor for the company. The terms of engagement of the professional accountant who was requested to prepare the 1982 financial statements did not include an audit, and an audit never was performed. In fact, the chairman of the finance committee directed the accountant not to perform the audit function, contrary to the by-laws, the C.B.C.A. and the best interests of the Government of the N.W.T.

10. Operations Shutdown

Observation

The shutdown of Delta Fur operations was not satisfactorily administered by the Department. The financial and legal position of Delta Fur in relation to its apparent insolvent financial position was not taken into account. Also, the loan agreement and debenture that had been signed by the company with the Commissioner was not put into effect.

The regional office, with the concurrence of Delta Fur's board of directors, decided to close operations on December 23, 1982, due to the company's evidently insurmountable financial problems. Quite properly, inventories were taken at shutdown by regional office and Delta Fur staff. Efforts were made by regional staff to move merchandise inventory and collect accounts receivable.

However, Delta Fur's default in paying the government's fur issues, and its apparent insolvent financial position, did not cause the Department to invoke the terms of the loan and debenture agreements. Professional accounting and legal advice was not sought before payments were made to creditors after December 23, 1982.

Furthermore, synoptic journals and the general ledger were left unposted with respect to transactions that occurred following the December, 1982, shutdown. The company bank accounts came under the control of the Area Economic Development Officer. Deposits, disbursements and transfers after shutdown were subject to his direction with no effective second party control.

After January, 1983, most of the company's payments were made by bank drafts instead of by company **cheque**. Sales were not recorded, journal entries were not prepared and source documentation was inadequate. Therefore, internal control over transactions after shutdown was unsatisfactory.

The Department's headquarters staff involvement was conspicuously absent shortly before, during and after shutdown on December 23, 1982. This was not in keeping with headquarters' responsibilities toward Delta Fur.

Recommendation

We recommend the preparation of a policy, together with explanatory procedures which would provide adequate direction for Department staff when involved in the financial affairs of an enterprise.

11. Estimated Investment in Delta Fur

Observation

The government's investment in Delta Fur was an inefficient use of funds for the purpose of creating employment.

We estimated that the total cost to the government over the past four years, with respect to its involvement in Delta Fur, exceeded \$938,000. This amount was determined by taking into account the following direct and indirect costs:

Inventory transfer	\$212,000
Revolving fund write-down	172,000
Professional fees	195,000
Assistance to Industry contribution	125,000
Interest on revolving fund	154,000 (1)
Accounts receivable write-off	80,000
Department time & travel	?
Arctic Marketing Enterprises	<u>?</u>
Estimated minimum investment	<u><u>\$938,000</u></u>

(1) Interest was calculated on the actual monthly balance at an annual rate of 10%.

As the Department did not maintain a record of direct and indirect costs, none of the elements of this estimate are necessarily complete.

A departmental memorandum dated January 26, 1979, apprised the Executive Committee about the studies which were to lead to the Delta Fur proposal. That memorandum included the following comment:

"The second phase consisted of an analysis of costs and revenues associated with various employment and production levels, together with alternative product mixes to determine whether the shops could be operated with the requirement that any government subsidies necessary would not exceed the value of the wage bill."

The analysis to which the memorandum referred concluded that government subsidies would amount to substantially less than the wage bill.

We determined that local wages amounted to \$483,000 over the period of Delta Fur's operations. Therefore, the direct and indirect government subsidies of at least \$938,000 exceeded wages by a ratio of almost two to one.

Recommendation

We recommend that the Department maintain a complete and comprehensive record of all costs associated with undertakings of this nature.

12. Production Equipment

Observation

The fur production equipment used **by** Delta Fur was leased from the Aklavik and Nanuk Co-operatives for a nominal \$2.00 per year. We counted the equipment during our audit visit to the shops and found discrepancies between the items on hand and the inventory as scheduled on the lease agreement (Schedules I and J refer).

This leased equipment and additional equipment noted on the schedules should not be construed as a complete inventory. **At** the time we counted **and** recorded the equipment on hand we did not have any knowledge of the **lease** agreement. Therefore, some of the minor items listed in the lease schedule were not necessarily counted and recorded during our audit visit. Furthermore, the equipment may not be released to the co-operatives as it may be tied up due to Delta Fur's financial insolvency.

It should also be noted that the regional office removed the fur sewing machine heads from the Aklavik shop in order to better secure this equipment in the regional warehouse.

Recommendation

We recommend that:

- a) the equipment be recounted;
- b)** any major items remaining and not well secured be moved to the regional warehouse or otherwise secured;
- c) the legal aspects of this equipment be determined and acted upon as required.

Acknowledgement

We would like to thank the Department's regional and headquarters staff for their co-operation during the performance of this audit.

A handwritten signature in cursive script, appearing to read 'D. Hill'.

D. Hill

Executive Manager

DELTA FUR COMPANY LIMITEDIndex

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Schedule J	Physical Inventory Results - Shop Equipment (Tuktoyaktuk)

DELTA FUR
 ACCOUNTS RECEIVABLE
 AS **AT** JANUARY 31, 1984

	<u>Balance</u>
Alberta Vocational Centre	\$ 5,043.81
Terry Anderson	80.00
Cec Corrigal Fur Clinic Ltd.	765.00
Evergreen Jewellery	3,120.00
Hudsons Bay Co. Ltd.	1,467.13
Husky Insurance	750.00
Glen Hovey	8,794.78
Majestic Fashions	3,120.00
Northern Images (N.W.T.)	22,993.00
Northern Images (Yukon)	6,585.00
O.T. Tannery Shop	2,675.00
Place of Man	6,750.00
Shoes and Things	1,450.00
Toa Chen's Gallery	60.00
Union Village Flower Shop	<u>1,560.00</u>
	65,213.72
Less:	
Allowance for doubtful accounts (Note)	
(75% x 65,213.72)	<u>(48,910.29)</u>
Balance	<u><u>\$16,303.43</u></u>

NOTE : **A 75%** factor for doubtful accounts was arbitrarily decided upon. The accounts are all over two years old.

DELTA FUR
ACCOUNTS PAYABLE
AS AT JANUARY 31, 1984

	<u>Balance</u>
Aklavik Air Ltd.	\$ 179.00
Petroleum Products Division GNWT	7,702.52
Richard, Vertes & Lang	1,084.85
Hamlet of Tuktoyaktuk	<u>93.42</u>
	<u>\$ 9,059.79</u>
 Receiver General of Canada	 <u>\$ 294.12</u>
 Government of the N.W.T. Revolving Fur Fund Payable	 <u>\$73,116.85</u>
 <u>Total Payable to the GNWT</u>	
Petroleum Products Division	\$ 7,702.52
GNWT Revolving Fur Fund	<u>73,116.85</u>
	<u>\$80,819.37</u>

DELTA FUR
SCHEDULE OF MONTHLY SALES (1)

<u>Month</u>	<u>Sales</u>	
April, 1980	\$ 88,436	
May " "	43,300	
June " "	24,961	
July " "	58,596	
Aug. " "	78,073	
Sept. " "	60,226	
Ott. " "	93,727	
Nov. " "	30,064	
Dec. " "	42,398	
Jan. 1981		(2)
Feb. " "	35,590	
Mar. " "		(2)
	<hr/>	
Total Sales 80/81	\$555,371	(3)
	<hr/> <hr/>	
April, 1981	\$ 12,529	
May " "	12,599	
June " "	4,112	
July " "		(2)
Aug. " "		(2)
Sept. " "	34,038	
Ott. " "	21,860	
Nov. " "	3,374	
Dec. " "	30,920	
Jan. 1982	3,036	
Feb. " "	3,376	
Mar. " "	22,447	
	<hr/>	
Total Sales 81/82	\$148,291	(3)
	<hr/> <hr/>	
April, 1982	\$ 13,834	
May " "	5,495	
June " "	2,589	
July " "	14,867	
Aug. " "	23,439	
Sept. " "	11,777	
Oct. " "	21,869	
Nov. " "	21,878	
Dec. " "	64,548	
Jan. 1983	2,004	
Misc. sales for 1982-83	45,946	
	<hr/>	
Total Sales 82/83	\$228,246	
	<hr/> <hr/>	

NOTES : (1) Sales were taken from the Sales Journal.
(2) No sales were recorded in the Sales Journal.
(3) Total sales did not agree to the sales reported
in the 1981 and 1982 financial statements.

DELTA FUR COMPANY LIMITED
BALANCE SHEET
AS AT MARCH **31, 1982**

(UNAUDITED - PREPARED BY D. JORSTEAD C.A.)

	<u>1982</u>	<u>Restated 1981</u>
<u>ASSETS</u>		
CURRENT		
Cash	\$ 200	\$183,746
Term deposits		87,191
Accounts receivable	7,994	22,051
Employee advances	2,961	
Inventory	206,423	238,025
Prepaid expenses	4,871	
	<u>222,449</u>	<u>531,013</u>
FIXED	5,347	1,059
	<u>\$227,796</u>	<u>\$532,072</u>
<u>LIABILITIES</u>		
CURRENT		
Bank overdraft	\$ 3,513	\$ -
Accounts payable and accrued	25,055	26,303
Employee deductions payable	18,715	5,234
Government of the N.W.T.		
- Revolving Fur Fund	73,1107	188,069
	<u>120,380</u>	219,606
DUE GOVERNMENT OF THE NORTHWEST TERRITORIES	<u>334,469</u>	<u>334,469</u>
<u>SHAREHOLDERS' DEFICIENCY</u>		
SHARE CAPITAL	2	2
DEFICIT	<u>(227,055)</u>	<u>(22,005)</u>
	<u>\$227,796</u>	<u>\$332,072</u>

APPROVED BY THE BOARD:

_____ Director
_____ Director

DELTA FUR COMPANY LIMITED
LOSS
AS AT MARCH 31, 1982

(UNAUDITED - PREPARED BY D. JORSTEAD C.A.)

	<u>1982</u>	<u>Restated 1981</u>
REVENUE		
Sales	\$ 172,800	\$647,167
Cost of goods sold	<u>252,219</u>	<u>579,356</u>
Gross margin	<u>(79,419)</u>	<u>67,811</u>
OVERHEAD EXPENSES		
Administrative salaries	47,303	33,066
Rent and utilities	27,931	6,782
Bad debts	32,024	16,756
Travel	9,839	15,862
Interest and bank charges	3,822	770
Shop supplies	3,748	10,043
Professional fees	2,397	10,113
Office	2,133	5,588
Communications	1,970	3,843
Insurance	1,415	3,388
Advertising	975	1,286
Repairs and maintenance	372	5,095
Depreciation and amortization	<u>712</u>	<u> </u>
	<u>134,641</u>	<u>112,592</u>
OPERATING LOSS	<u>(214,060)</u>	<u>(44,781)</u>
Interest on term deposits	<u>9,010</u>	<u>22,776</u>
NET LOSS	<u><u>\$(205,050)</u></u>	<u><u>\$(22,005)</u></u>

SCHEDULE OF REVOLVING FUND FUR INVENTORY TRANSACTIONS

<u>Month</u>	<u>Opening Balance</u>	<u>Government Fur Purchases</u>	<u>Fur Issues to Delta Fur</u>	<u>Closing Balance</u>
April, 1980	\$300,851	\$ -	\$ -	\$300,851
May "	300,851	101,993	58,285	344,559
June "	344,559	103,238		447,797
July "	447,797	6,063	84,629	369,231
August "	369,231	837		370,068
Sept. "	370,068	29,195	58,152	341,111
Oct. "	341,111			341,111
Nov. "	341,111	884	62,893	279,102
Dec. "	279,102		38,160	240,942
Jan. 1981	240,942			240,942
Feb. "	240,942	1,205	34,980	207,167
Mar. "	207,167	120,885		328,052
Apr. "	328,052	526		328,578
May "	328,578	43,151		371,729
June "	371,729			371,729
July "	371,729			371,729
Aug "	371,729	905		372,634
Sept. "	372,634			372,634
Oct. "	372,634	15,643		388,277
Nov. "	388,277	410	74,312	314,375
Dec. "	314,375	238		314,613
Jan. 1982	314,613			314,613
Feb. "	314,613			314,613
Mar. "	314,613	105,395	41	419,967
Apr. "	419,967	551		420,518
May "	420,518			420,518
June "	420,518	19,568		440,086
July "	440,086			440,086
Aug. "	440,086			440,086
Sept. "	440,086	1,656		441,742
Ott. "	441,742	54		441,796
Nov. "	441,796			441,796
Dec. "	441,796	354		442,150
Jan. 1983	442,150	6,708		448,858
Feb. "	448,858			448,858
Mar. "	448,858			448,858

Source: Inuvik Region Government Services

AKLAVIK SHOP EQUIPMENT
 ACTUAL COUNT COMPARED TO LEASE
 AS AT NOVEMBER 30, 1983

<u>Equipment Description</u>	<u>Number Per Lease</u>	<u>Number Per Count 11/83</u>	<u>Difference Over/(Short)</u>
Judy	1	?	?
Fur drum machine	1	1	
Steam-Gen. c/w iron	1	1	
Singer sew. math. c/w table	1	1	
Mitsubishi sew. math. c/w table	1	1	
Bonis fur machines:			
a) c/w heads & table	7	1	(6) (1)
b) heads only	4	5	1
Allenbrook Hashfield sew. math.	1		(1)
Singer blind stitch c/w table	1	1	
Green tool box	1	1	
Unitrex F2082 (adding math.)	1		(1)
Sentry safe	1	1	
4 drawer legal file	1	1	
IBM Typewriter	1	1	
Metal cabinets (3 drawer)		2	2
Wooden desks		4	4
Typewriter table		1	1
Swivel chair		1	1
Sheffield fur math. head		1	1 (1)
Fur machine tables		7	7 (1)
Sewing machine table		1	1
Electric scissors		2	2
Pinking shears		1	1

NOTES :

- (1) The net result of the count is that four heads remain unaccounted for .
- (2) We did not have the lease and attached equipment schedules at the time the inventory was performed. Accordingly we concentrated primarily on fur sewing equipment.

TUKTOYAKTUK SHOP EQUIPMENT
ACTUAL COUNT COMPARED TO LEASE
AS AT NOVEMBER 30, 1983

<u>Equipment Description</u>	<u>Number Per Lease</u>	<u>Number Per Count 11/83</u>	<u>Difference Over/(Short)</u>
Victor adding machine (damaged)	1	?	?
Sentry safe	1	destroyed	(1) (1)
Legal filing cabinet	1	1	
Royal Typewriter (manual)	1	?	?
Cash bill dispenser	3	?	?
Blind stitch basting machine	1		(1)
Bonis fur machine c/w table:			
Model A16	4	10	2 (3)
B27	4		
Allenbrook-Hashfield sewing machine	2		(2) (2)
Bonis fur drum	1	1	
Iron & boiler	1	1	
Portable blower kleenbit	1	1	
Step ladder	1	1	
Judy	4	4	
Brothers sewing machine		2	2 (2)
Serving table		1	1

NOTES :

- (1) Safe was forced open during audit visit in order to determine contents, this rendered the safe completely useless (scrap).
- (2) There is no actual shortage of sewing machines; rather there has been a switch in brands from Allenbrook-Hashfield to Brothers.
- (3) Bonis fur machines are over by (2); these may have been transferred from the Aklavik Shop.
- (4) Items with question mark (?) may be in inventory; we primarily concentrated on fur equipment as we did not have the lease and its equipment schedules at the time of our audit visit.

DELTA FUR COMPANY LIMITED

Collection Follow-up I terns

Additional items which require further development and collection action have been included in this appendix for the Department's information. These items represent potential recoveries to Delta Fur and in turn to the government.

Our working papers contain much of the necessary support that would be useful in following-up and facilitating collection.

1. Cash

- a) A deposit made up on May **14, 1982**, in the amount of **\$5,003.50, was** lost by Delta Fur; however, there is a copy of the deposit which lists the amounts and makers of the cheques. The regional office has been doing some follow-up.
- b) When the Delta Fur safes were opened in November, **1983**, a number of **undeposited** stale-dated cheques(1981) amounting to \$440.00 were found. Follow-up has been left with the regional office.
- c) A Visa charge for \$60.00 which was processed as Mastercard on December 7, 1982, was returned and never redirected. 'The originals were sent along with our **November 16, 1983**, memorandum to the regional office for processing and follow-up.

2. Payroll Taxes

According to the evidence in Delta Fur's files, there may have been a \$7,776.66 overpayment to Revenue Canada for payroll taxes. We have had discussions with appropriate Revenue Canada staff and have received an incomplete detail listing of Delta Fur's account from them. The information that was provided continues to confirm that an overpayment had been made.

3. Elizabeth Kunnizzie

- a) A balance of \$2,500 is still outstanding from a payroll advance intended to be used to purchase furniture.
- b) On December 24, 1982, the day after Delta Fur ceased operations, Ms. **Kunnizzie** made out a cheque to herself for **\$1,000**, apparently for vacation pay. However, she had taken vacation in **June**, 1982, according to the payroll records. We were unable to determine if she was entitled to more vacation after June, 1982.

4. Accounts Receivable

Delta Fur's accounts receivable collection activity warrants full time attention. Presently, the regional office is following up on outstanding accounts as time permits.