

Natural Capital Investment Fund, Inc.

Financial Report
December 31, 2018

Contents

Independent auditor's report	1-2
<hr/>	
Financial statements	
Statement of financial position	3
Statement of activities	4
Statement of functional expenses	5
Statement of cash flows	6
Notes to financial statements	7-27

Independent Auditor's Report

To the Board of Directors
Natural Capital Investment Fund, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Natural Capital Investment Fund, Inc. (NCIFund), which comprise the statement of financial position as of December 31, 2018, the related statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the financial statements (collectively, financial statements).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of NCIFund as of December 31, 2018, and the changes in its net assets and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the financial statements, in 2018 NCIFund adopted new accounting guidance Accounting Standards Update 2016-14, *Not-for-Profit Entities (Topic 958) Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

Other Reporting Required by Government Auditing Standards

In accordance with *Governmental Auditing Standards*, we have also issued our report dated June 20, 2019, on our consideration of NCIFund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of NCIFund's internal control over financial reporting or on compliance. The report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering NCIFund's internal control over financial reporting and compliance.

RSM US LLP

Blue Bell, Pennsylvania
June 20, 2019

Natural Capital Investment Fund, Inc.

**Statement of Financial Position
December 31, 2018**

Assets	
Current assets:	
Cash and cash equivalents	\$ 10,664,659
Accounts receivable	18,034
Promises to give	315,140
Loans receivable, net of allowance for loan losses of \$264,314	5,286,287
Contracts receivable	18,435
Accrued interest and fees receivable	187,027
Total current assets	16,489,582
Noncurrent assets:	
Cash - restricted	1,577,011
Cash equivalents held as collateral	42,000
Other asset	202,600
Investment (U.S. Endowment Fuel Project)	99,995
Loans receivable, net of allowance for loan losses of \$1,924,508	27,879,905
Total noncurrent assets	29,801,511
Total assets	\$ 46,291,093
Liabilities and Net Assets	
Current liabilities:	
Accounts payable	\$ 89,966
Line of credit	150,000
Accounts payable, related party	1,742,727
Funds held for others	13,269
Current maturities of secured borrowings, participations	173,587
Accrued interest payable	67,718
Current maturities of notes payable	273,239
Total current liabilities	2,510,506
Revolving line of credit, related party	5,000,000
Secured borrowings, participations	2,024,462
Notes payable	17,184,315
Subordinated notes payable	3,292,118
Total noncurrent liabilities	27,500,895
Total liabilities	30,011,401
Commitments and contingencies (Note 12)	
Net assets:	
Without donor restrictions	9,990,768
With donor restrictions	6,288,924
Total net assets	16,279,692
Total liabilities and net assets	\$ 46,291,093

See notes to financial statements.

Natural Capital Investment Fund, Inc.

**Statement of Activities
Year Ended December 31, 2018**

	Without Donor Restrictions	With Donor Restrictions	Total
Financial activity:			
Financial income:			
Loan interest revenue	\$ 1,982,469	\$ -	\$ 1,982,469
Fee income on loans	171,630	-	171,630
Interest income	100,687	-	100,687
Total financial income	2,254,786	-	2,254,786
Financial expenses:			
Provision for loan losses	1,167,348	-	1,167,348
Interest expense	669,459	-	669,459
Total financial expenses	1,836,807	-	1,836,807
Net financial income	417,979	-	417,979
Revenue and support:			
Grants and contributions	13,720	694,656	708,376
Government grants	-	1,812,434	1,812,434
Project income	73,542	73,739	147,281
Other income	34,131	-	34,131
Net assets released from restriction	1,989,124	(1,989,124)	-
Total revenue and support	2,110,517	591,705	2,702,222
Expenses:			
Program services:			
Lending	1,393,750	-	1,393,750
Strategic initiatives	830,004	-	830,004
Total program services	2,223,754	-	2,223,754
Supporting services:			
Management and general	208,075	-	208,075
Fundraising	57,439	-	57,439
Total supporting services	265,514	-	265,514
Total expenses	2,489,268	-	2,489,268
Change in net assets	39,228	591,705	630,933
Net assets:			
Beginning of year	9,951,540	5,697,219	15,648,759
End of year	\$ 9,990,768	\$ 6,288,924	\$ 16,279,692

See notes to financial statements.

Natural Capital Investment Fund, Inc.

**Statement of Functional Expenses
Year Ended December 31, 2018**

	Program Services		Total Program	Supporting Services		Total
	Lending	Strategic Initiatives		Management and General	Fundraising	
Management fee contract **	\$ 1,141,487	\$ 402,072	\$ 1,543,559	\$ 148,131	\$ 51,037	\$ 1,742,727
Provision for loan losses	1,167,348	-	1,167,348	-	-	1,167,348
Interest expense	669,459	-	669,459	-	-	669,459
Grant and contract expense	-	221,651	221,651	-	-	221,651
Technical assistance	-	155,827	155,827	-	-	155,827
Loan origination expense	61,900	-	61,900	-	-	61,900
Employee travel	42,064	16,022	58,086	9,326	2,034	69,446
Computer software maintenance services	40,547	15,444	55,991	8,989	1,960	66,940
Office expense	17,408	6,631	24,039	3,859	841	28,739
Loan workout expense - non-legal	27,826	-	27,826	-	-	27,826
Rent	15,719	5,987	21,706	3,485	760	25,951
Professional fees	-	-	-	21,494	-	21,494
Conference, convention, meeting	8,919	3,397	12,316	1,977	431	14,724
Legal fees	11,561	-	11,561	-	-	11,561
Debt acquisition costs	11,276	-	11,276	-	-	11,276
Bank charges	-	-	-	9,084	-	9,084
Marketing	4,733	1,803	6,536	1,049	229	7,814
Reporting and filing fees	7,239	-	7,239	-	-	7,239
Employee training and development	3,071	1,170	4,241	681	147	5,069
	<u>\$ 3,230,557</u>	<u>\$ 830,004</u>	<u>\$ 4,060,561</u>	<u>\$ 208,075</u>	<u>\$ 57,439</u>	<u>\$ 4,326,075</u>

See notes to financial statements.

** Management Fee Contract – NCIFund contracts with its parent company, The Conservation Fund (TCF), to provide certain administrative support services as well as hiring all NCIFund employees. Accordingly, TCF is paid for actual costs associated with NCIFund staff salaries, benefits management and an allocated portion of indirect support costs. The contractual agreement for 2018 was \$1,742,727.

Natural Capital Investment Fund, Inc.

**Statement of Cash Flows
Year Ended December 31, 2018**

Cash flows from operating activities:	
Increase in net assets	\$ 630,933
Adjustments to reconcile increase in net assets to net cash provided by operating activities:	
Provision for loan losses	1,167,348
Implied interest expense	90,723
Contributions restricted for long-term purposes	(337,625)
Changes in operating assets and liabilities:	
Accounts receivable	(2,525)
Promises to give	(56,586)
Accrued interest and fees receivable	(54,944)
Accounts payable	46,942
Accounts payable, related party	276,337
Funds held for others	5,825
Accrued interest payable	6,948
Net cash provided by operating activities	1,773,376
Cash flows from investing activities:	
Cash disbursements on loans receivable	(11,688,722)
Principal collections on loans receivable	4,266,464
Proceeds from sale of OREO	73,716
Net cash used in investing activities	(7,348,542)
Cash flows from financing activities:	
Proceeds from issuance of notes payable	7,757,904
Repayments of notes payable	(804,802)
Advances on secured borrowings, participations	1,313,152
Repayments on secured borrowings, participations	(41,340)
Contributions restricted for long-term purposes	337,625
Net cash provided by financing activities	8,562,539
Net increase in cash and cash equivalents	2,987,373
Cash and cash equivalents:	
Beginning of year	9,296,297
End of year	\$ 12,283,670
Cash and cash equivalents - unrestricted	\$ 10,664,659
Cash - restricted	1,577,011
Cash equivalents held as collateral	42,000
	\$ 12,283,670
Supplemental disclosure of cash flow information:	
Cash paid for interest	\$ 571,788
Supplemental schedule of noncash investing activities:	
Loans receivable transferred to OREO	\$ 73,716

See notes to financial statements.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies

Natural Capital Investment Fund, Inc. (NCIFund) is a certified community development financial institution that provides financing for and technical assistance to natural resource-based businesses. NCIFund's base is in West Virginia, but it also conducts lending and investing activities in North Carolina, portions of South Carolina and Georgia, and the Appalachian counties in Maryland, Virginia, Tennessee, Ohio, and Kentucky.

NCIFund's activities include the following two program areas:

Lending program: NCIFund is a specialized, niche lender for start-up and early stage small businesses in underserved markets. The primary goal of its loan programs is to create or retain full-time private sector jobs. NCIFund provides microloans in amounts from \$1,000 to \$50,000 and business loans sized from \$50,000 to \$750,000. NCIFund is approved as a United States Department of Agriculture (USDA) Business & Industry (B & I) Guaranteed Lender, giving it the ability to participate in transactions up to \$2.5 million.

NCIFund's business clients are predominantly located in economically distressed rural communities and are unable to access capital from traditional sources. Target sectors include, but are not limited to: environmental services, local food system infrastructure, heritage and recreation-based tourism, value-added agriculture, renewable energy, energy efficiency, recycling, water conservation and treatment, secondary forest products, natural medicines, green building, critical community services, and technologies that support the sustainable use of natural resources.

NCIFund pursues Triple Bottom Line (TBL) small business development as a means to responsibly create wealth in distressed communities. Small and mid-sized businesses can demonstrate the viability of utilizing natural assets responsibly, while offering opportunities in low income communities to build wealth through the creation of living wage jobs with benefits and skill building opportunities. While NCIFund specializes in financing TBL companies, it recognizes that economically and environmentally healthy communities require a diverse range of businesses and services, so NCIFund expanded its work.

Strategic initiatives program: NCIFund's strategic initiatives use targeted funding and partnerships with small business-related or sector-specific community partners to devote added resources to particular sectors or constituencies within NCIFund's stated mission. These initiatives frequently combine NCIFund's loan capital with a) targeted business advisory services and/or b) grant funding from partners in order to ensure borrower success and "buy down" the cost of critical infrastructure or services for the constituencies NCIFund seeks to serve.

Basis of presentation: NCIFund prepares its financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP), which have been applied on a consistent basis and follow general practices within the nonprofit industry. A description of the net asset classes is as follows:

Net assets without donor restrictions: All resources over which the governing board has discretionary control. The governing board of the NCIFund may elect to designate such resources for specific purposes. This designation may be removed at the Board's discretion.

Net assets with donor restrictions: Net assets subject to donor- (or certain grantor-) imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Restriction will be released when the requirements of the donor or grantor have been satisfied through expenditure for the specified purpose of the program or through the passage of time.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor contributions to be used for loan capital are recorded by NCIFund in its Loan Capital Revolving Fund as perpetual in nature. The funds are used to provide financing capital to qualifying businesses. The Loan Capital Revolving Fund is replenished as the loan principal is repaid. In the event that a note receivable funded by contributions that are perpetual in nature, becomes uncollectible, NCIFund writes off the uncollectible amount (loss) against the net assets.

Cash and cash equivalents: NCIFund classifies cash, money market funds, and sweep accounts with original maturities of ninety days or less as cash and cash equivalents. The cash held in the sweep account is held in U.S. government money market fund, which is recorded at cost which approximates fair value.

Restricted cash: In order to secure its obligations in existing loan agreements, NCIFund is required to maintain certain bank accounts and balances, wherein the proceeds of the loans shall be held in separate custodial accounts established at a mutually acceptable financial institution. This requirement includes two federal programs, two financial institution lenders and one private lender. For the Intermediary Relending Program (IRP) which includes the Rural Microentrepreneur Assistance Program (RMAP), NCIFund agrees to deposit in a custodial account on the closing date the full amount of the proceeds of the loan and thereafter, principal or proceeds received by the ultimate recipient, and all interest, dividends or other earnings. The amounts deposited in the account shall not be commingled with any other funds. In addition, IRP, RMAP and the Small Business Administration (SBA) require cash to be restricted for loan loss reserves as described in the allowance for loan loss policy on the following page. A private lender requires NCIFund to hold a loan loss reserve and the same lender also holds a loan loss reserve in the same amount. See Note 2.

Cash equivalents held as collateral: In order to meet certain private lenders' requirements for loans receivable, NCIFund records certificates of deposit as collateral. The certificates of deposit are held at cost and have short-term maturities.

Investment: NCIFund holds investments in the U.S. Endowment Fuel Project. NCIFund provided two investments totaling \$99,995 to finance fuel stations in logging communities in South Carolina for the members of a certain cooperative. NCIFund earns minimal revenues on fuel sold.

Promises to give: Unconditional contributions, including unconditional promises to give, are recognized at fair value as support in the period received. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Conditional promises to give are recognized when the conditions on which they depend are substantially met. Management determines the allowance for doubtful promises by regularly evaluating individual promises to give and considering the prior history of the donor and proven collectability of past donations. Promises to give are written off when deemed uncollectible. Recoveries of promises to give previously written off are recorded when received. There was no allowance for doubtful promises at December 31, 2018.

Loans receivable: NCIFund makes small business loans to customers. These loans are made in West Virginia, North Carolina and the Appalachian and rural areas of Maryland, Ohio, Kentucky, Tennessee, Virginia, South Carolina and Georgia. The ability of NCIFund's debtors to honor their contracts is dependent upon general economic conditions in the respective area.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

Loans receivable are stated at the principal amount outstanding, net of allowance for losses. Interest income on loans is accrued on the principal outstanding at the loans' stated interest rate unless the loan is in default. Related direct loan origination fees and costs are deferred and amortized over the life of the loans; however, as NCIFund has determined that direct loan origination fees and costs are not significant, NCIFund does not record them. Fees relating to expired commitments are recognized as non-interest income. If a commitment is exercised during the commitment period, the fee at the time of exercise is recognized over the life of the loan as an adjustment of yield.

Loans are considered past due if the required principal and interest payments have not been received 30 days from the date such payments were due. If it otherwise appears doubtful that the loan will be repaid or if the cash flow of the business can only support a principal payment, management may place the loan on nonaccrual status. Generally, loans on non-accrual status are 90 days or more past due and are moving toward foreclosure/liquidation.

Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for loan losses: The allowance for loan losses is a valuation reserve that management believes will be adequate to absorb possible losses on existing loans that may become uncollectible. It is established through a provision for loan losses charged to expense. In addition, loans deemed to be uncollectible are charged against the allowance. The allowance is based upon management's periodic review of the collectability of loans and is maintained at a level believed adequate by management to absorb estimated potential losses after considering changes in internal and external factors, past loss experience, the nature and volume of the portfolio and current economic conditions. However, the allowance is an estimate that could change if there are significant changes in the portfolio and/or economic conditions.

A specific reserve component is calculated for watch list loans by assessing the probability of default, which is determined based on internal factors such as borrower financial position strength, lien position, charge-offs, and non-accruals; together with external factors like national and local economic conditions and industry trends.

The IRP requires a 6% general reserve on loans issued on its program which of \$327,094 at December 31, 2018 and is included in the allowance for loan losses. NCIFund also maintains a 6% cash reserve on IRP loans of \$86,229 at December 31, 2018, which is classified with restricted cash.

The RMAP requires a 5% general reserve on loans issued on its program which of \$4,129 at December 31, 2018 and is included in the allowance for loan losses. NCIFund also maintains a 5% cash reserve on RMAP loans of \$7,484 at December 31, 2018, which is classified with restricted cash.

The Small Business Administration (SBA) 7A program requires the establishment of cash loan reserves equal to 5% and 3%, respectively, of the unguaranteed and guaranteed portion of the SBA 7A portfolio. The required balance reserve at December 31, 2018 was \$6,096 and reported with restricted cash. The balance of the loan reserve at December 31, 2018 was \$6,799 and reported with the allowance for loan losses.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

Impaired loans: A loan is considered impaired when, based on current information and events, it is probable that NCIFund will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the original loan agreement and the loan has a high probability of moving into foreclosure/liquidation. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan or lease and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is generally measured on a case-by-case basis using the fair value of the collateral, if the loan is collateral dependent, the present value of expected future cash flows discounted at the loans effective interest rate or the loan's observable market price.

Troubled debt restructures (TDR): A loan that was restructured where the lender granted a concession that otherwise it would not consider due to the borrower's financial difficulties. The concession would allow for continued albeit lower or less frequent payments.

Other real estate owned (OREO): Real estate acquired through foreclosure is carried at estimated fair value, less estimated costs of disposal. Costs of improving OREO are capitalized to the extent that the carrying value does not exceed its fair value less estimated selling costs. Holding costs are charged to period expense. Gains and losses on sales, if any, are recognized in financial income (loss) as they occur.

Notes payable: NCIFund uses debt primarily for financing for natural resource-based businesses. Most debt is in the form of notes payable to foundations, financial institutions, and various government agencies. NCIFund records a discount and contribution revenue when note interest rates are considered below-market and amortizes the discount to interest expense over the term of the related notes.

Transfers of financial assets: Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (1) the assets have been isolated from NCIFund, (2) the transferee obtains the right to pledge or exchange the transferred assets and no condition both constrains the transferee from taking advantage of that right and provides more than a trivial benefit for the transferor, and (3) the transferor does not maintain effective control over the transferred assets through either (a) an agreement that both entitles and obligates the transferor to repurchase or redeem the assets before maturity or (b) the ability to unilaterally cause the holder to return specific assets, other than through a cleanup call.

NCIFund sells participation loans to third parties that do not meet the criteria to be accounted for as sales as NCIFund has not surrendered control of the participation loans sold. As a result the participation loans are accounted for as secured borrowings, whereby NCIFund records cash received from the transferee and records a liability to repay the cash to the transferee. The transferees have no recourse to NCIFund for failure of the underlying borrowers to pay amounts contractually due. The outstanding balance of participation loans sold accounted for as secured borrowings is \$2,198,049 as of December 31, 2018.

Revenue recognition: NCIFund's primary revenues come from interest and fees earned on loans originated in connection with the execution of loans to third parties. These revenues are without donor restrictions and are an integral part of the funding of NCIFund operations. Interest income on loans is recognized over the term of the loan and is calculated using the simple interest method on principal amounts outstanding.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

NCIFund also receives funding for its programs from federal grants and from corporations and foundations in the form of operating grants. NCIFund recognizes contributions received, including unconditional promises to give, as support in the period received. Contributions received are reported as support with or without donor restrictions.

Promises to contribute that stipulate conditions to be met before the contribution is made to NCIFund are not recognized until the conditions are met.

Functional allocation of expenses: The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Management and general expenses, such as the management fee, rent, employee travel and training, and other office expenses that support programs are allocated to the programs based on full-time employee salaries and a percentage of time worked on program-specific duties.

Income taxes: NCIFund is generally exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code. In addition, NCIFund qualifies for charitable contribution deductions and has been classified as an organization that is not a private foundation. Income which is not related to exempt purposes, less applicable deductions, is subject to federal and state corporate income taxes. NCIFund had no net unrelated business income tax for the year ended December 31, 2018.

Management evaluated NCIFund's tax positions and concluded that NCIFund had taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance. NCIFund files income tax returns in the U.S. federal jurisdiction. Generally, NCIFund is no longer subject to income tax examinations for the U.S. federal, state or local tax authorities for the years before 2015.

Use of estimates: The preparation of financial statements in conformity with U.S. GAAP requires management to make a number of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates made by management include the allowance for loan losses. Actual results could materially differ from those estimates.

Adopted accounting pronouncements: In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The amendments in this ASU make improvements to the information provided in financial statements and accompanying notes of not-for-profit entities. The amendments set forth the FASB's improvements to net asset classification requirements and the information presented about a not-for-profit entity's liquidity, financial performance and cash flows. NCIFund adopted the ASU for the year ended December 31, 2018.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force)*, which provides guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. NCIFund adopted the ASU for the year ended December 31, 2018.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

Recent accounting pronouncements not yet adopted: In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which establishes a comprehensive revenue recognition standard for virtually all industries in U.S. GAAP, including those that previously followed industry-specific guidance. In August 2015, the FASB issued ASU 2015-14, which defers the effective date of ASU 2014-09 for all entities by one year. The new standard is effective for annual reporting periods beginning after December 15, 2018. NCIFund is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

In January 2016, FASB issued ASU 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01 includes a number of amendments that address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. NCIFund has not yet determined the effect on the financial statements of adopting the amendments included in ASU 2016-01.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in Topic 840, *Leases*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the statement of financial position for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the statement of activities. The new standard is effective for annual reporting periods beginning after December 15, 2019. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. NCIFund is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

In April 2016, the FASB issued ASU 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*. ASU 2016-10, clarifies two aspects of Topic 606 – identifying performance obligations and the licensing implementation guidance. The ASU is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. NCIFund is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

In May 2016, the FASB issued ASU 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*. This ASU addresses various implementation issues by making narrow-scope amendments to the guidance originally included in ASU 2014-09 and providing practical expedients. The ASU is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. NCIFund is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which creates a new credit impairment standard for financial instruments. The existing incurred loss model will be replaced with a current expected credit loss (CECL) model for both originated and acquired financial instruments carried at amortized cost and off-balance sheet credit exposures, including loans, loan commitments, held-to-maturity debt securities, financial guarantees, net investment in leases, and most receivables. Recognized amortized cost financial assets will be presented at the net amount expected to be collected through an allowance for credit losses. Expected credit losses on off-balance-sheet credit exposures will be recognized through a liability. Unlike current guidance, which requires certain favorable changes in expected cash flows to be accreted into interest income, both favorable and unfavorable changes in expected credit losses (and therefore the allowance) will be recognized through credit loss expense as they occur. With the exception of purchased financial assets with a more than insignificant amount of credit deterioration since origination, for which the initial allowance will be added to the purchase price of the assets, the initial allowance on financial assets subject to the scope (whether originated or acquired) will be recognized through credit loss expense. Expanded disclosures will also be required. The ASU is effective for fiscal years beginning after December 15, 2021. NCIFund is currently evaluating the impact of adopting this new guidance on its financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 provides guidance on how certain cash receipts and cash payments should be presented and classified in the statement of cash flows with the objective of reducing existing diversity in practice with respect to these items. ASU 2016-15 is effective for annual periods, and interim periods within those years, beginning after December 15, 2018. NCIFund is currently evaluating the impact the adoption of this guidance will have on its statements of cash flows.

In December 2016, the FASB issued ASU 2016-20, *Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers*. This ASU makes certain changes to the new revenue recognition guidance added to the FASB's Accounting Standards Codification by ASU 2014-09. The ASU is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. NCIFund is currently evaluating the impact of the adoption of this guidance on its financial statements.

In June 2018, the FASB issued ASU 2018-08, *Nonprofit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. This ASU clarifies the guidance for evaluating whether a transaction is reciprocal (i.e., an exchange transaction) or nonreciprocal (i.e., a contribution) and for distinguishing between conditional and unconditional contributions. The ASU also clarifies the guidance used by entities other than nonprofits to identify and account for contributions made. The ASU has different effective dates for resource recipients and resource providers. Where NCIFund is a resource recipient, the ASU is applicable to contributions received for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Where NCIFund is a resource provider, the ASU is effective for annual periods beginning after December 15, 2019, and interim periods within annual periods beginning after December 15, 2020. Early adoption is permitted. NCIFund is currently evaluating the impact of the adoption of this guidance on its financial statements.

In July 2018, the FASB issued ASU 2018-10, *Codification Improvements to Topic 842, Leases*. This ASU clarifies and corrects unintended application of narrow aspects of the lease accounting guidance. For entities that early-adopted Topic 842, the amendments are effective upon issuance of ASU 2018-10, and the transition requirements are the same as those in Topic 842. For entities that have not adopted Topic 842, the effective date and transition requirements for ASU 2018-10 are the same as the effective date and transition requirements in Topic 842 (for annual reporting periods beginning after December 15, 2019 for NCIFund). NCIFund is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies (Continued)

In July 2018, the FASB issued ASU 2018-11, *Leases (Topic 842): Targeted Improvements*. This ASU (a) allows entities to initially apply ASC 842 at the adoption date and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption; and (b) provides a practical expedient under which lessors may elect, by class of underlying assets, to not separate nonlease components from the associated lease component. For entities that have not adopted Topic 842 before the issuance of ASU 2018-11, the effective date and transition requirements for the amendments related to separating components of a contract are the same as those in ASU 2016-02. For entities that have adopted Topic 842 before the issuance of ASU 2018-11, the practical expedient for separating components may be elected either in the first reporting period following the issuance of ASU 2018-11 or at the original effective date of Topic 842 for that entity. NCIFund is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

Note 2. Cash and Cash Equivalents

Cash and cash equivalents held by NCIFund at December 31, 2018 consist of the following:

Cash	\$ 2,316,214
U.S. government money market fund	9,925,456
	<u>\$ 12,241,670</u>
Unrestricted cash and cash equivalents	\$ 10,664,659
Restricted cash	1,577,011
	<u>\$ 12,241,670</u>

Restricted cash balances at December 31, 2018 are held for the following purposes:

Revolving loan funds:	
Intermediary Relending Program	\$ 806,249
Rural Microentrepreneur Assistance Program	61,293
	<u>867,542</u>
Cash required to be segregated by lender:	
Financial institution lenders	318,693
Private lender	190,967
	<u>509,660</u>
Cash loan loss reserves:	
Intermediary Relending Program	86,229
Private lender - held by lender	50,000
Private lender - held by NCIF	50,000
Rural Microentrepreneur Assistance Program	7,484
Small Business Administration	6,096
	<u>199,809</u>
	<u>\$ 1,577,011</u>

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 3. Other Asset

NCIFund holds two certificate of deposits (CDs) that are associated with a third party; one CD is for \$174,600 and the other CD is for \$28,000. The CDs are in the name of NCIFund but are assigned as collateral to a bank that has two loans totaling approximately \$1 million with the third party. In the event of default in the bank's loans, the bank would cash in the CDs and apply them to the balance of the bank's loans. Then, NCIFund would have two loans with the third party for \$174,600 and \$28,000.

Note 4. Promises to Give

As of December 31, 2018, unconditional promises to give totaling \$315,140 are due in less than one year. At December 31, 2018, NCIFund also had ten conditional promises to give totaling \$2,650,291.

Note 5. Loans Receivable

Loans receivable consist primarily of loans made to small businesses at December 31, 2018 as follows:

Loans receivable	\$ 35,355,014
Less allowance for loan losses	2,188,822
Loans receivable, net	<u>\$ 33,166,192</u>

Loans carry remaining terms of less than 1 year to 22 years and carry interest rates of 0.5% to 8.0%. The loans are generally payable in monthly or quarterly installments of either interest-only (non-amortizing) or principal and interest (amortizing) over the term of each loan.

The following is a summary of lien priority on loans held by NCIFund at December 31, 2018:

Lien position:	Number of Loans	Gross Loans	Allowance for Loan Losses	Net Loans
Unsecured	4	\$ 162,942	\$ (8,147)	\$ 154,795
Secured	215	35,192,072	(2,180,675)	33,011,397
	<u>219</u>	<u>\$ 35,355,014</u>	<u>\$ (2,188,822)</u>	<u>\$ 33,166,192</u>

Loans are primarily secured by the underlying assets financed, such as real estate, equipment, and inventory.

Loans receivable totaling \$2,483,822 and restricted cash of \$806,249 serve as collateral on IRP notes payable at December 31, 2018. Loans receivable totaling \$73,397 and restricted cash of \$61,293 serve as collateral on RMAP notes payable at December 31, 2018.

Accrued interest receivable amounted to \$185,812 at December 31, 2018.

Non-accrual loans totaled \$684,022 at December 31, 2018.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 5. Loans Receivable (Continued)

Aging: The following table represent an aging of loans as of December 31, 2018. The table presents the principal amount outstanding on the loans that may be past due for principal and/or interest payments contractually due:

	30 - 60 Days Past Due	61 - 90 Days Past Due	91+ Days Past Due	Total Past Due	Current	Total Loans
Business loans	\$ 484,858	\$ -	\$ 1,215,667	\$ 1,700,525	\$ 33,654,489	\$ 35,355,014

Credit quality: Management uses internally assigned risk ratings as indicators of credit quality. Each loan's risk rating is assigned at origination and updated at least annually and more frequently if circumstances warrant a change in risk rating. NCIFund uses a loan grading system that follows its loan policy.

In evaluating the credit risk of the NCIFund's loan portfolio, management has developed an internal credit risk rating system based on a variety of risk factors that they believe represent leading indicators of credit quality. The NCIFund's internal credit risk ratings are categorized as 1 through 7, with the lowest credit risk rating representing the highest quality financing receivables.

RR 1 – Strong: Loans categorized as RR 1 exhibit extremely high credit quality, with virtually no perceived credit risk, as evidenced by very strong cash flow, net worth, working capital, quality collateral and management.

RR 2 – Low Risk: Loans categorized as RR 2 exhibit high credit quality, as evidenced by strong cash flow, an abundance of quality collateral, and borrowers with stable management and seasoned loan payment histories.

RR 3 – Acceptable Risk: Loans categorized as RR 3 exhibit normal credit quality profiles, with acceptable overall credit characteristics related to capital, asset quality, management, earnings, and liquidity.

RR 4 – Moderate Risk/Start-Up: Loans categorized RR 4 exhibit identified some credit concerns (e.g., start-up with no proven performance, etc.), which warrant increased monitoring, but not necessarily expected to result in credit loss.

RR 5 – High Risk: Loans categorized RR 5 exhibit deterioration in overall credit quality, such that some level of credit loss is reasonably expected to occur.

RR 6 – Problem Asset: Loans categorized RR 6 exhibit significant deterioration in overall credit quality and collateral position is weak or non-existent. The loan is not performing as agreed and has been delinquent for at least 90 days or more. Current conditions indicate that full repayment is highly questionable or unlikely. NCIFund is moving toward writing off the loan.

RR 7 – Written Off: Loans that have been determined are not collectible and will be written off.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 5. Loans Receivable (Continued)

The following table summarizes the loan portfolio by internal credit risk rating at December 31, 2018:

1 - Strong	\$	-
2 - Low Risk		3,745,788
3 - Acceptable Risk		17,846,513
4 - Moderate Risk/Start-Up		12,249,013
5 - High Risk		409,716
6 - Problem Asset		883,433
7 - Written Off		220,551
	<u>\$</u>	<u>35,355,014</u>

Allowance for loan losses: The following is an analysis of the allowance for loan losses for the year ended December 31:

Beginning balance	\$	1,431,844
Provision charged to operations		1,167,348
Less charge-offs		410,370
Ending balance	<u>\$</u>	<u>2,188,822</u>
Allowance for loan losses allocated:		
Individually evaluated for impairment	\$	403,413
Collectively evaluated for impairment		1,785,409
	<u>\$</u>	<u>2,188,822</u>
Loans receivable:		
Individually evaluated for impairment	\$	684,022
Collectively evaluated for impairment		34,670,992
	<u>\$</u>	<u>35,355,014</u>

Impaired loans: The following is an analysis of impaired loans for which a specific reserve component has been calculated for the year ended December 31, 2018:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Business loans	<u>\$ 684,022</u>	<u>\$ 684,022</u>	<u>\$ 403,413</u>	<u>\$ 684,022</u>	<u>\$ 38,351</u>

Troubled debt restructures: As of December 31, 2018, the outstanding principal balance of troubled debt restructures was \$1,793,632. The associated allowance for loan losses for troubled debt restructures was \$535,237 as of December 31, 2018. During the year ended December 31, 2018, five loans were modified and considered to be troubled debt restructures. The loans had pre-modification balance and post-modification balance of \$614,688. The modifications in 2018 included rate reductions and extension of maturity dates. There were no unfunded commitments on troubled debt restructures as of December 31, 2018.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 6. Investments and Fair Value Measurements

In accordance with accounting guidance on fair value measurements, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the measurement date.

In determining fair value, management uses various valuation approaches, as may be appropriate in the circumstance, including market, income and or cost approaches. Accounting guidance establishes a fair value hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset developed based on market data obtained from sources independent of NCIFund. Unobservable inputs are those that reflect management's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1:** Valuations based on unadjusted quoted prices in active markets for identical assets that management has the ability to access. Valuation adjustments and block discounts are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.
- Level 2:** Valuations based on inputs that are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies. At December 31, 2018, management determined that all of its investments measured at fair value fell into this category.
- Level 3:** Valuations based on inputs that are unobservable and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment and estimation.

The availability of valuation techniques and observable inputs can vary from instrument to instrument and is affected by a wide variety of factors, including, for example, the type of instrument, whether the instrument is new and not yet established in the marketplace, and other characteristics particular to the transaction. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Those estimated values do not necessarily represent the amounts that may be ultimately realized due to the occurrence of future circumstances that cannot be reasonably determined.

Because of the inherent uncertainty of valuation, those estimated values may be materially higher or lower than the values that would have been used had a ready market for the securities existed.

Fair value is a market-based measure considered from the perspective of a market participant who holds the asset or owes the liability rather than an entity-specific measure. Therefore, even when market assumptions are not readily available, management's own assumptions are set to reflect those that market participants would use in pricing the asset or liability at the measurement date.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 6. Investments and Fair Value Measurements (Continued)

U.S. Endowment Fuel Project: NCIFund has investments in the U.S. Endowment Fuel Project in the amount of \$99,995 at December 31, 2018, which are considered investments held at cost.

Fair Value on a Nonrecurring Basis

Impaired loans: The fair value of impaired loans is determined based on the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. The valuation allowance for impaired loans is included in the allowance for losses in the statement of financial position. The valuation allowance for impaired loans at December 31, 2018 was \$403,413.

	Level 1	Level 2	Level 3	Total
Impaired loans	\$ -	\$ -	\$ 280,609	280,609
	\$ -	\$ -	\$ 280,609	\$ 280,609

Note 7. Related Party Transactions

NCIFund has entered into a management services agreement with its parent organization, TCF. Under the terms of the agreement, TCF provides certain staffing and administrative services to NCIFund. The management fee under the agreement was \$1,742,727 for the year ended December 31, 2018 and this amount is payable as of December 31, 2018. The agreement is for one year and is renewable for successive one-year terms unless either party provides written notice not to renew.

TCF provides a \$5,000,000 revolving line of credit to NCIFund to help finance its short-term capital needs. The balance outstanding as of December 31, 2018 was \$5,000,000. Also see Note 9.

On March 15, 2018, TCF provided another \$2,000,000 revolving line of credit to NCIFund for additional financing. There is no outstanding balance at December 31, 2018. Also see Note 9.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 8. Notes Payable and Subordinated Notes Payable

Notes payable consist of the following at December 31, 2018:

Lender		Undrawn Amounts	Balance
U.S. Department of Agriculture - IRP	Six notes are payable over a 30-year term with 1% simple interest. Payments of principal and interest are due annually. Secured by funds held by NCIF under the IRP and collateral obtained as a result of advancing loan funds. One note from 2014 includes an implied interest rate of 3% with a remaining discount of \$54,673.	\$ 365,625	\$ 2,389,676
U.S. Department of Agriculture - RMAP	Note is payable over a 20 year term with 2% simple interest. Monthly principal and interest payments began 2 years after closing date with Year 1 and Year 2 interest capitalized to the principal balance. Secured by funds held by NCIF under the RMAP program and collateral obtained as a result of advancing loan funds.	375,000	125,559
West Virginia Infrastructure & Jobs Development Council	Used as matching funds for the U.S. Department of Agriculture loan. Includes two notes payable each over a 15-year term with interest at 1% per annum. Quarterly principal and interest payments due on the notes until maturity February 2020 and January 2026. Secured on a pro rata basis with USDA loan on funds held by NCIF under the IRP.	-	183,560
West Virginia Infrastructure & Jobs Development Council	Used as matching funds for the U.S. Department of Agriculture loan. Note is payable over a 15-year term, with interest at 3% per annum. Monthly principal and interest payments due on the note until maturity June 2033. Secured on a pro rata basis with USDA loan on funds held by NCIF under the IRP.	362,125	135,269
	Total secured notes payable		2,834,064
Mary Reynolds Babcock Foundation	Principal payments are deferred for 10 years. Simple interest of 2% is due semi-annually in arrears over 10 years. The implied interest rate is 3% resulting in a remaining discount of \$5,911. The principal sum plus final interest payment is payable at the end of 10 years on August 2023.	-	744,089
One Foundation	Note matures December 2025. Interest only payments starting in March 2016 through December 2018 at the rate of 2%. After which, principal and interest shall be paid quarterly of \$3,836 until note maturity.	-	100,000
McKnight Foundation	Note matures May 2028. Refinanced note with additional funds borrowed. Simple interest of 2% paid annually. Yearly principal payments of \$500,000 begin May 1, 2025, the 7th anniversary of the note closing and continue until note is paid.	-	2,000,000
Appalachian Community Capital	Note matures June 2020. Floating interest is based on its cost of funds plus 1% payable monthly. Interest rate at December 31, 2018 was 3.55%	-	2,000,000

(Continued)

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 8. Notes Payable and Subordinated Notes Payable (Continued)

Lender		Undrawn Amounts	Balance
Ford Foundation PRI	Note matures January 2021. Note is payable over a 10-year term, with principal payments deferred for 7 years. Remaining annual principal payments of \$666,667 due in Years 9 and 10. Interest is payable at the rebate of 1% per annum, with an implied interest rate of 3% resulting in a remaining discount of \$38,959	\$ -	\$ 1,294,374
Coastal Enterprises, Inc.	Note matures December 2022. Note is payable over a 10-year term, with principal payments deferred for 7 years. Annual principal repayments begin after 7 years with payments of approximately one-third each year for 3 years. Interest is payable at a rate of 4%. The lender holds \$50,000 as collateral as described in Note 3.	-	1,000,000
Franconia II 2012 Trust	Note matures September 2021. General recourse balloon note payable in 4 years with simple interest payments only of 2.5% due quarterly in arrears over 4 years.	-	75,000
Laughing Gull Foundation	Consists of three notes all maturing in April 2020. Notes are over 4-year term for the full principal balance and all accrued interest. Interest is payable quarterly at the rate of 2% every January 31st, April 30th, July 31st and October 31st for the term of the notes.	-	500,000
Fresh Pond Capital	This investment firm relationship is made up of ten individual impact investors. Notes range from \$50,000 to \$250,000 and mature between August 2020 and October 2022. Notes are payable over 4-year terms for the full principal balance. Simple interest is payable quarterly at 2%	-	1,025,000
Giant Steps Foundation	Note matures September 2022 and is payable over 5-year term for the full principal balance and all accrued interest. Interest is payable at a rate of 2.5% quarterly during the term of the note.	-	25,000
One Foundation POWER	Note matures September 30, 2027. Note is payable over a 10-year term with interest only payments through September 30, 2022. Principal and interest payments for the remaining 5 years. Interest is payable at the rate of 2% quarterly during the term of the note.	-	300,000
PNC Bank	Note matures October 2020 and is payable over 3-year term for the full principal balance and all accrued interest. Interest is payable at the rate of 3.75% quarterly during the term of the note.	-	1,000,000

(Continued)

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 8. Notes Payable and Subordinated Notes Payable (Continued)

Lender		Undrawn Amounts	Balance
Woodforest Bank	Note matures May 2023 and is payable over 7-year term with interest only paid monthly until March 2019 at the rate of 3%. Thereafter principal and interest payments are due monthly during the term of the note.	\$ -	\$ 500,000
Mercy Investment Services	Note matures on March 2023. Simple interest of 3% paid quarterly. The principal sum plus final interest payment is payable at the end of the note.	-	500,000
Loring Wolcott & Coolridge Trust	Note matures on April 2023. Simple interest of 2.25% paid annually. The principal sum plus final interest payment is payable at the end of the note.	-	50,000
Seton Fund	Note matures on April 2023. Simple interest of 3%. Principal and interest due quarterly with a \$75,000 balloon payment due April 2023.	-	139,452
Eastern WV Community Foundation	Note matures on September 2023. Simple interest of 3.5% paid annually. The principal sum plus final interest payment is payable at the end of the note.	-	200,000
New Vision Treatment	Note matures on September 2022. Simple interest of 3%. Quarterly principal and interest payments due monthly until maturity.	-	70,575
H. Shott Foundation	Note matures on August 2023. Simple interest of 2% due annually. The principal sum plus final interest payment is payable at the end of the note.	-	100,000
Northern Trust	Note matures on July 2023. Simple interest of 2% due semi-annually. The principal sum plus final interest payment is payable at the end of the note.	-	2,000,000
Appalachian Community Capital	Note matures on September 2021. Floating interest is based on its cost of funds plus 1% payable monthly. The interest rate at December 31, 2018 was 3.34%.	-	1,000,000
		<u>\$ 1,102,750</u>	<u>17,457,554</u>
	Less current portion		<u>273,239</u>
	Noncurrent portion		<u>\$ 17,184,315</u>

(Continued)

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 8. Notes Payable and Subordinated Notes Payable (Continued)

Subordinated notes payable consist of the following at December 31, 2018:

Lender		Balance
Wells Fargo	Equity-equivalent debt investment maturing August 2020. Payable in 10 years with simple interest payments of 2% due quarterly in arrears over 10 years. The implied interest rate is 3%, resulting in a remaining discount of \$7,882.	\$ 392,118
Wells Fargo ENC	Equity-equivalent debt investment maturing May 2028. Simple interest only payments of 2% due quarterly for the first 10 years. Thereafter quarterly principal payments due of \$125,000 quarterly for the last two years until the end of the note.	1,000,000
United Bank	Equity-equivalent debt investment maturing January 2029. Simple interest only payments of 2% due quarterly for the first 10 years. Thereafter quarterly principal payments due of \$62,500 quarterly for the last two years until the end of the note.	500,000
PNC Community Development Company	Equity-equivalent debt investment note, with interest payable quarterly starting July 1, 2015 and continuing on the first day of each quarter until maturity. Interest is payable at the rate of 3% per annum. Payment of the principal amount is due and payable upon maturity of the note on April 1, 2020. Issuer may exercise one five-year extension to extend the maturity to April 1, 2025.	500,000
Capital Bank	Equity-equivalent debt investment note with an initial target maturity date of October 2023. Bank has option of extending maturity date. Simple interest of 3.5 % payable quarterly. The principal sum plus final interest payment is payable at the end of the note.	400,000
United Bank	Equity equivalent debt investment note maturing January 2030. Simple interest only payments of 2% due quarterly for the first 10 years. Thereafter quarterly principal payments due of \$62,500 quarterly for the last two years until the end of the note.	500,000
	Total subordinated notes payable	\$ 3,292,118

U.S. GAAP requires interest expense and contribution revenue to be reported in connection with loans of cash to not-for-profit organizations that are interest free or that have below-market interest rates. The contribution is recognized at the time the loan is made and amortized using the effective interest method. The accretion increases interest expense and notes payable. Implied interest discount was \$107,425 at December 31, 2018.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 8. Notes Payable and Subordinated Notes Payable (Continued)

Aggregate annual principal payments applicable to notes payable and subordinated notes payable in future fiscal years is as follows:

Years ending December 31:	
2019	\$ 273,239
2020	6,388,435
2021	2,416,037
2022	1,024,855
2023	4,389,492
Thereafter	6,365,039
	<u>\$ 20,857,097</u>

Subordinated notes payable: NCIFund has entered into equity equivalent transactions with financial institutions as a way to increase its lending capacity and also protect its senior lenders. These equity equivalents are reflected above and in the statement of financial position as subordinated notes payable. The notes represent a general obligation of NCIFund and are not secured by any of the entity's assets. They are fully subordinate to the right of repayment of all other creditors and do not allow for acceleration of repayment except in very limited circumstances.

NCIFund is subject to a number of restrictive financial and non-financial covenants in its notes payable agreements, such as minimum net asset requirements, current liquidity ratios, loan performance ratios and other various leverage ratios. Audit financial statements are required to be submitted between 90 and 180 days depending on the lender. NCIFund did not meet the requirement to submit audited financial statements for those between 90 and 150 days, however, it received waivers from those lenders.

Note 9. Revolving Lines of Credit

NCIFund has obtained a \$5,000,000 revolving line of credit from its parent, TCF, to help finance its short-term capital needs. Interest is payable quarterly on outstanding balances at an interest rate of 2%. Any outstanding principal and accrued interest will be payable on August 1, 2020. The amount outstanding from the line amounted to \$5,000,000 at December 31, 2018.

On March 15, 2018, NCIFund obtained an additional \$2,000,000 revolving line of credit from TCF for additional financing. Interest is payable quarterly on outstanding balances at an interest rate of 2.5%. Any outstanding principal and accrued interest will be payable on March 1, 2023. There were no amounts drawn on the line as of December 31, 2018.

NCIFund maintains a \$150,000 revolving line of credit with a lending institution, to be drawn upon as needed, with a variable rate equal to 0.250 percentage points below The Wall Street Journal Prime Rate, which shall not be more than 7% or less than 3% as of calendar year end. Interest is payable quarterly, with all unpaid principal and interest due at maturity on June 7, 2019. The total outstanding balance was \$150,000 at December 31, 2018.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 10. Concentrations of Credit Risk

NCIFund maintains its cash in various banks. The bank account balances, at times, may exceed federally insured limits set by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 for the years ended December 31, 2018 and 2017. As of December 31, 2018, NCIFund's cash and money market fund balances in excess of FDIC-insured amounts totaled \$10,486,734. NCIFund has not experienced any losses with these accounts. Management believes NCIFund is not exposed to any significant credit risk on domestic cash balances.

During 2018, federal grant revenue accounted for 67% of NCIFund's revenue and support. During 2018, NCIFund's expenses incurred to TCF accounted for 40% of total expenses.

Note 11. Net Assets With Donor Restrictions

Net assets with donor restrictions are those net assets whose use by NCIFund is limited by the donors for a special purpose or restricted to be used in a later period. At December 31, 2018, donor restricted net assets consisted of the following:

Restricted for specified purpose:

Loan capital \$ 1,114,084

Provide support for business development to natural resource-based enterprises and provide incentives to businesses to engage in sound environmental practices

1,341,721

2,455,805

Perpetual in nature:

Restricted for specified purpose:

Loan capital revolving fund

Represents net assets dedicated to providing temporary financing to qualified businesses

3,833,119

\$ 6,288,924

Note 12. Commitments and Contingencies

NCIFund is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the statement of activities.

NCIFund's exposure to credit loss is represented by the contractual amount of these commitments. NCIFund follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

At December 31, 2018, the following financial instruments were outstanding whose contract amounts represent credit risk:

Loan commitments approved not disbursed \$ 3,282,478

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments for lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by NCIFund, is based on management's credit evaluation of the customer.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 12. Commitments and Contingencies (Continued)

Unfunded commitments under commercial lines of credit and revolving credit lines are commitments for possible future extensions of credit to existing customers. These lines of credit are uncollateralized and ultimately may not be drawn upon to the total extent to which NCIFund is committed.

NCIFund participates in a number of federal grant and contract programs which are subject to financial and compliance audits. Accordingly, NCIFund's compliance with applicable grant or contract requirements may be determined at some future date. The amount, if any, of expenditures which may be disallowed by the granting or contracting agencies cannot be determined at this time, although management expects such amounts, if any, to be immaterial.

As more fully described in Note 3, NCIFund holds two CDs that support a third party loan made by a bank. If the loan with the bank defaults, the bank would cash in the CDs and apply them to the balance of the bank's loans. Then, NCIFund would have two loans with the third party for \$174,600 and \$28,000.

Note 13. Liquidity and Availability of Financial Resources

NCIFund financial assets available within one year of December 31, 2018 for general expenditures are as follows:

Cash and cash equivalents - unrestricted	\$	10,664,659
Cash - restricted		1,577,011
Cash equivalents held as collateral		42,000
Accounts receivable		18,034
Promises to give		315,140
Loans receivable, net		33,166,192
Contracts receivable		18,435
Accrued interest and fees receivable		187,027
Long-term investment (U.S. Endowment Fuel Project)		99,995
Total financial assets		<u>46,088,493</u>
Cash - restricted		(1,577,011)
Cash equivalents held as collateral		(42,000)
Donor restricted funds		(6,288,924)
Notes receivable, due after one year, net		(27,879,905)
Notes receivable due in next year restricted for federal relending program		(146,676)
Long-term investment (U.S. Endowment Fuel Project)		(99,995)
Outstanding loan commitments, not disbursed		<u>(3,282,478)</u>
Amounts not available to be used within one year		<u>(39,316,989)</u>
Financial assets available to meet general expenditures within one year	\$	<u>6,771,504</u>

NCIFund is also supported by restricted programmatic funds that can be used to support programmatic and general expenditures. Because a donor's restriction requires funds to be used in a particular manner or in a future period, NCIFund must maintain sufficient resources to meet those responsibilities.

Natural Capital Investment Fund, Inc.

Notes to Financial Statements

Note 13. Liquidity and Availability of Financial Resources (Continued)

NCIFund has a goal to maintain unrestricted cash and cash equivalents to equal or exceed three months of cash operating expenses, which are, on average, approximately \$700,000. In addition, as a part of its liquidity management, NCIFund invests cash in excess of daily requirements in a U.S. government money market fund. In the event of an unanticipated liquidity need, NCIFund could obtain a bank line of credit.

Note 14. Subsequent Events

Management evaluated subsequent events through June 20, 2019, the date the financial statements were available to be issued.

On March 1, 2019, NCIFund wired \$1,742,727 to TCF to pay off the related party payable outstanding at December 31, 2018.

On March 19, 2019, NCIFund executed a note payable agreement to borrow \$1,000,000 from Opportunity Finance Network at an interest rate of 4% per annum. Principal is due at maturity on March 31, 2024.

On March 28, 2019, NCIFund received a conditional grant for \$250,000 to capitalize a revolving loan fund from an existing donor to finance catalytic commercial real estate projects and small businesses which support downtown revitalization of coal impacted communities. The initial installment of \$31,250 was received on April 11, 2019 and the remaining will be paid upon satisfaction of conditions of reporting and satisfactory progress.

On March 29, 2019, NCIFund wired \$1,049,863 to TCF as principal payment on the \$5,000,000, revolving line of credit. On April 10, 2019, NCIFund wired an additional principal payment for \$250,000.

On April 1, 2019, NCIFund executed a note payable agreement to borrow \$250,000 from Fresh Pond Capital at an interest rate of 2% per annum. Principal is due at maturity on March 31, 2024.

On April 30, 2019, NCIFund executed an unsecured note payable agreement to borrow \$300,000 from Greater Kanawha Valley Foundation at a fixed interest rate of 2% per annum. Interest is paid annually with principal due at maturity on April 30, 2024.