

NEWTEK BUSINESS SERVICES INC

Form 10QSB

November 14, 2003

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# SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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## FORM 10-QSB

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2003

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

Commission File Number: 001-16123

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# NEWTEK BUSINESS SERVICES, INC.

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(Exact name of registrant as specified in its charter)

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New York

11-3504638

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(State or other jurisdiction of  
incorporation or organization)

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(I.R.S. Employer  
Identification No.)

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100 Quentin Roosevelt Boulevard, Garden City, NY

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11530

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(Address of principal executive offices)

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(Zip Code)

Registrant's telephone number, including area code: (516) 390-2260

Check whether the registrant has (1) filed all documents and reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety days. Yes  No

As of November 12, 2003, 25,097,485 shares of Common Stock were issued and outstanding.

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**Table of Contents****ITEM 1. FINANCIAL STATEMENTS****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)**

	<b>September 30, 2003</b>	<b>December 31, 2002</b>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 35,000,307	\$ 41,171,358
Credits in lieu of cash	73,411,999	41,580,950
SBA loans receivable (net of reserve for possible SBA loan losses of \$1,690,964 as of September 30, 2003)	50,623,424	56,073,016
SBA loans held for sale	804,440	
Accounts receivable (net of allowance of \$169,798 and \$34,466, respectively)	664,107	661,351
Receivable from bank	2,489,608	2,938,309
Accrued interest receivable	215,877	285,151
Investments in qualified businesses held to maturity investments	2,592,568	3,962,353
Investments in qualified businesses equity investments	300,000	1,091,110
Structured insurance product	3,014,355	2,893,301
Prepaid insurance	12,673,214	14,056,196
Prepaid expenses and other assets	1,774,813	575,772
Furniture, fixtures and equipment (net of accumulated depreciation of \$327,926 and \$190,590, respectively)	729,274	546,231
Customer merchant accounts	3,208,838	356,675
Goodwill	3,225,353	2,862,965
<b>Total assets</b>	<b>\$ 190,728,177</b>	<b>\$ 169,054,738</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>Liabilities:</b>		
Accounts payable and accrued expenses	\$ 5,178,789	\$ 4,218,367
Notes payable certified investors	3,833,525	3,844,181
Notes payable insurance	3,881,803	5,369,896
Notes payable other	2,365,183	480,500
Borrowings under line of credit		450,000
Bank notes payable	48,970,105	53,824,492
Interest payable in credits in lieu of cash	61,831,800	65,196,116
Deferred tax liability	12,582,824	3,726,151
<b>Total liabilities</b>	<b>138,644,029</b>	<b>137,109,703</b>
Minority interest	8,688,868	4,772,741

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Commitments and contingencies		
Stockholders' equity:		
Common Stock (par value \$0.02 per share; authorized 39,000,000 shares, issued and outstanding 25,948,889 and 25,341,428 not including 582,980 shares held in escrow, as of September 30, 2003 and December 31, 2002, respectively)	518,978	506,828
Additional paid-in Capital	23,262,523	20,992,827
Unearned Compensation	(98,334)	
Retained earnings	19,712,113	5,672,639
	<u>43,395,280</u>	<u>27,172,294</u>
Total stockholders' equity	43,395,280	27,172,294
	<u>\$ 190,728,177</u>	<u>\$ 169,054,738</u>
Total liabilities and stockholders' equity	\$ 190,728,177	\$ 169,054,738

See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)****FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002**

	Three Months Ended September 30,		Nine months Ended September 30,	
	2003	2002	2003	2002
<b>Revenue:</b>				
Income from tax credits	\$ 22,067,285	\$ 14,886,087	\$ 43,926,619	\$ 25,144,192
Credit card processing revenue	1,879,526	519,798	3,867,612	912,730
Interest and dividend income	921,507	78,329	3,005,227	683,016
Other income	1,141,963	1,250,581	2,815,815	1,318,098
Recovery of investment permanently written off	350,000		350,000	
Gain on sale of property				16,841
Consulting fee income	68,353	168,736	102,953	268,053
<b>Total revenue</b>	<b>26,428,634</b>	<b>16,903,531</b>	<b>54,068,226</b>	<b>28,342,930</b>
<b>Expenses:</b>				
Interest	3,322,298	3,090,193	10,526,385	8,658,556
Payroll and consulting fees	1,725,050	2,049,085	4,471,345	4,245,085
Credit card processing direct costs	870,932	318,675	2,393,580	521,313
Credit card processing administrative costs	1,227,443	431,202	2,252,204	1,341,503
Professional fees	691,991	902,837	2,748,647	2,427,007
Insurance	622,731	471,609	1,834,148	1,336,364
Other than temporary decline in value of investments	257,339	601,025	1,991,040	1,588,630
Equity in net losses of affiliates		120,993		793,868
Provision for SBA loan losses	(7,429)		331,371	
Other	955,093	812,640	2,898,486	1,511,133
<b>Total expenses</b>	<b>9,665,448</b>	<b>8,798,259</b>	<b>29,447,206</b>	<b>22,423,459</b>
<b>Income before minority interest, provision for income taxes, extraordinary gain on acquisition of minority interest and extraordinary gain on acquisition of a business</b>				
	16,763,186	8,105,272	24,621,020	5,919,471
Minority interest in (loss) income	(1,231,560)	689,952	(1,911,602)	1,738,590
<b>Income before provision for income taxes and extraordinary gain</b>	<b>15,531,626</b>	<b>8,795,224</b>	<b>22,709,418</b>	<b>7,658,061</b>
Provision for income taxes	(6,057,334)	(3,342,186)	(8,856,673)	(2,910,064)
<b>Income before extraordinary gain on acquisition of minority interest and extraordinary gain on acquisition of a business</b>	<b>9,474,292</b>	<b>5,453,038</b>	<b>13,852,745</b>	<b>4,747,997</b>
Extraordinary gain on acquisition of minority interest, net of taxes of \$162,778 for 2002				265,584
Extraordinary gain on acquisition of a business			186,729	
<b>Net income</b>	<b>\$ 9,474,292</b>	<b>\$ 5,453,038</b>	<b>\$ 14,039,474</b>	<b>\$ 5,013,581</b>

See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)****FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002 (CONTINUED)**

	Three Months Ended September 30,		Nine months Ended September 30,	
	2003	2002	2003	2002
Weighted average common shares outstanding:				
Basic	25,709,700	24,787,535	25,671,712	23,947,116
Diluted	26,110,536	24,847,408	26,016,931	24,052,620
Income per share:				
Basic	\$ 0.37	\$ 0.22	\$ 0.55	\$ 0.21
Diluted	\$ 0.36	\$ 0.22	\$ 0.54	\$ 0.21
Income per share before extraordinary items:				
Basic	\$ 0.37	\$ 0.22	\$ 0.54	\$ 0.20
Diluted	\$ 0.36	\$ 0.22	\$ 0.53	\$ 0.20

See accompanying notes to these unaudited condensed consolidated financial statements.



**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002**

	<u>September 30,</u> <u>2003</u>	<u>September 30,</u> <u>2002</u>
Cash flows from operating activities:		
Net income	\$ 14,039,474	\$ 5,013,581
Adjustments to reconcile net income to net cash used in operating activities:		
Other than temporary decline in value of investments	1,991,040	1,588,630
Gain on sale of asset held for sale		(16,841)
Equity in net losses of affiliates		793,868
Extraordinary gain on acquisition of minority interests		(265,584)
Extraordinary gain on acquisition of a business	(186,729)	
Income from tax credits	(43,926,619)	(25,144,192)
Deferred income taxes	8,856,673	2,910,064
Depreciation and amortization	258,940	90,922
Provision for SBA loan losses	331,371	
Proceeds from sale of SBA loans	2,438,119	
Accretion of interest income	(121,054)	(131,711)
Accretion of interest expense	8,642,249	8,066,217
Compensation expense for vested stock options	124,583	570,000
Issuance of stock for services received	58,388	80,789
Minority interest	1,911,602	(1,738,590)
Changes in assets and liabilities:		
Prepaid insurance	1,471,982	100,336
Prepaid expenses, accounts receivable and other assets	(348,270)	(316,080)
Accounts payable and accrued expenses	585,422	591,119
Net cash used in operating activities	<u>(3,872,829)</u>	<u>(7,807,472)</u>
Cash flows from investing activities:		
Proceeds from sale of asset held for sale		348,770
Investments in cost method investments	(55,000)	
Investments in qualified businesses (held to maturity)	(300,000)	(1,204,942)
Investments in qualified businesses (consolidated entities)	(9,510,000)	(9,295,667)
Return of principal held to maturity investments	469,855	4,902,566
Return of principal consolidated entities	4,206,675	8,677,906
Consolidation of majority owned partner companies	5,303,325	2,838,519
SBA loans issued	(3,724,500)	
Cash paid for acquisition of AMS	(1,500,000)	
Repayments of SBA loans receivable	5,589,916	
Cash received from AMS and Exponential acquisition, respectively	7,000	106,642
Purchase of furniture, fixtures and equipment	(320,379)	(223,590)
Net cash provided by investing activities	<u>166,892</u>	<u>6,150,204</u>

See accompanying notes to these unaudited condensed consolidated financial statements.



**Table of Contents****NEWTEK BUSINESS SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) (CONTINUED)**

	September 30, 2003	September 30, 2002
	<u>2003</u>	<u>2002</u>
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of debt	\$ 1,000,000	\$ 21,548,698
Principal repayments of note payable insurance	(1,488,093)	(11,640,982)
Principal repayments of mortgage payable		(306,929)
Net proceeds from issuance of common stock	1,393,641	1,898,499
Proceeds from exercise of stock options	243,042	
Distributions to CAPCO members		(7,867)
Contributions from members	6,000	
Proceeds from sale of preferred stock of subsidiary	2,000,000	
Principal repayment on notes payable to others	(315,317)	
Proceeds from issuance of warrants		572,298
Principal repayments of bank notes payable	(4,854,387)	(4,813,955)
Principal repayments of line of credit	(450,000)	(575,000)
	<u>                    </u>	<u>                    </u>
Net cash (used in) provided by financing activities	(2,465,114)	6,674,762
	<u>                    </u>	<u>                    </u>
Net (decrease) increase in cash and cash equivalents	(6,171,051)	5,017,494
Cash and cash equivalents beginning of period	41,171,358	31,171,966
	<u>                    </u>	<u>                    </u>
Cash and cash equivalents end of period	\$ 35,000,307	\$ 36,189,460
	<u>                    </u>	<u>                    </u>
<b>Supplemental disclosure of non-cash financing activities:</b>		
Reduction of credits in lieu of cash and interest payable in credits in lieu of cash balances due to delivery of tax credits to certified investors	\$ 12,095,570	\$ 7,589,449
	<u>                    </u>	<u>                    </u>
Consolidation of investments previously accounted for under the equity method		\$ 537,083
	<u>                    </u>	<u>                    </u>
Acquisition of Exponential (net liabilities assumed)		\$ 10,978
	<u>                    </u>	<u>                    </u>
Acquisition of Automated Merchant Services (net liabilities assumed)		\$
	<u>                    </u>	<u>                    </u>
Issuance of common stock in connection with acquisition of Exponential		\$ 920,000
	<u>                    </u>	<u>                    </u>
Goodwill recognized in connection with acquisition of minority interests	\$ 362,388	\$ 873,173
	<u>                    </u>	<u>                    </u>
Acquisition of five Capcos minority interests		
Newtek Business Services common stock issued		\$ 1,868,583
Less, minority interests acquired		914,580
	<u>                    </u>	<u>                    </u>
Goodwill recognized		\$ 954,003
	<u>                    </u>	<u>                    </u>
Acquisition of three Capcos minority interests		

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Minority interests acquired		\$ 1,369,156
Less, Newtek Business Services common stock issued		940,794
		<u>                    </u>
Extraordinary gain recognized		\$ 428,362
		<u>                    </u>
Issuance of note in partial payment for insurance		\$ 2,000,000
		<u>                    </u>
Details of AMS acquisition:		
Assets acquired ( including customer merchant accounts valued at approximately \$2,910,000)	\$ 3,075,000	
Less: Liabilities assumed	160,000	
Less: Accrued acquisition costs (included in assets acquired)	215,000	
Less: Notes issued to seller	1,200,000	
		<u>                    </u>
Cash paid for acquisition	\$ 1,500,000	
		<u>                    </u>

See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****NOTE 1 SIGNIFICANT ACCOUNTING POLICIES****Basis of presentation and description of business**

The unaudited condensed consolidated financial statements of Newtek Business Services, Inc. and Subsidiaries (the Company or Newtek) included herein have been prepared by Newtek pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to SEC rules and regulations. The unaudited condensed consolidated financial statements of Newtek reflect, in the opinion of management, all adjustments necessary to present fairly the financial position of Newtek at September 30, 2003, the results of its operations for the three and nine month periods ended September 30, 2003 and 2002, and its cash flows for the nine month periods ended September 30, 2003 and September 30, 2002. All adjustments are of a normal recurring nature. These financial statements should be read in conjunction with the annual financial statements and notes thereto for the year ended December 31, 2002. The results of operations for the three and nine months ended September 30, 2003 are not necessarily indicative of the results of operations to be expected for the year ending December 31, 2003.

The following is a summary of each certified capital company (Capco) or Capco fund, state of certification and date of certification:

<b>Capco</b>	<b>State of Certification</b>	<b>Date of Certification</b>
WA (Wilshire Advisers)	New York	May 1998
WP (Wilshire Partners)	Florida	December 1998
WI (Wilshire Investors)	Wisconsin	October 1999
WLA (Wilshire Louisiana Advisers)	Louisiana	October 1999
WA II (Wilshire New York Advisers, II)	New York	April 2000
WNY III (Wilshire New York Partners, III)	New York	December 2000
WC (Wilshire Colorado Partners)	Colorado	October 2001

The State of Louisiana has authorized three Capco funds which are all a part of the WLA Capco (the first fund). The second, Wilshire Louisiana Partners II (WLP II), and the third, Wilshire Louisiana Partners III (WLP III), were formed in October 2001, and October 2002, respectively.

In general, the Capcos issue debt and equity instruments, generally warrants (Certified Capital), to insurance company investors (Certified Investors). The Capcos then make targeted investments (Investments in Qualified Businesses), as defined under the respective state statutes, or, Qualified Businesses), with the Certified Capital raised. Such investments may be accounted for as either consolidated subsidiaries, under the equity method or cost method of accounting, depending upon the nature of the investment and the Company's and/or the Capco's ability to control or otherwise exercise significant influence over the investee. Each Capco has a contractual arrangement with the particular state that legally entitles the Capco to receive (or earn) tax credits from the state upon satisfying quantified, defined investment percentage thresholds and time

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requirements. In order for the Capcos to maintain their state-issued certifications, the Capcos must make Investments in Qualified Businesses in accordance with these requirements. Each Capco also has separate contractual arrangements with the Certified Investors obligating the Capco to pay interest on the aforementioned debt instruments whether or not it meets the

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**NOTE 1 SIGNIFICANT ACCOUNTING POLICIES: (Continued)**

statutory requirements for Investments in Qualified Businesses. The Capco can satisfy this interest payment obligation, at the Capco's discretion, by delivering tax credits in lieu of paying cash. The Capcos have the right to deliver the tax credits to the Certified Investors. The Certified Investors have the right to receive and use the tax credits and would, in turn, use these tax credits to reduce their respective state tax liabilities in an amount usually equal to 100% (Louisiana Capco and the Louisiana second fund - 110%) of their certified investment. The tax credits can be utilized over a ten-year period at a rate of 10% (Louisiana Capco and Louisiana second fund- 11%) per year and in some instances are transferable and all can be carried forward.

On December 31, 2002, Newtek acquired a majority stake in a nonbank U.S. Small Business Administration ( SBA ) lender. As a nonbank SBA lender, the company (originally named Commercial Capital Corp., now named Newtek Small Business Finance ( NSBF )) originates, sells (in whole or in part) and services SBA loans to qualifying small businesses, which are partially guaranteed by the SBA. Newtek Small Business Finance sells the SBA guaranteed portion of such SBA loans to third-party investors, retains the unguaranteed portion and continues to service the SBA loans. Newtek Small Business Finance has the ability to originate SBA loans throughout the United States. Presently, the SBA loans originated by the company are primarily to customers in the Northeast United States. The Company's competition for originating SBA loans comes primarily from banking organizations and the other nonbank entities holding an SBA license.

**SBA Loans Receivable**

As of December 31, 2002, SBA loans that are past due more than 90 days, but were still performing (accruing interest), amounted to \$293,800. Of this amount, \$175,000 became current, and \$100,000 was moved to non-performing status. As of September 30, 2003, SBA loans that are past due more than 90 days, but are still performing (accruing interest), amount to \$65,824.

As of December 31, 2002, SBA loans that are on a non-accrual basis amounted to \$2,914,767. As of September 30, 2003, SBA loans that are on a non-accrual basis amount to \$4,248,724. This increase was predominately due to two SBA loans being downgraded to non-performing.

**Stock Based Compensation**

Newtek has elected to continue using Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, in accounting for employee stock options. No stock-based employee compensation cost is reflected in net income, as all options granted under the Company's plan had an exercise price equal to the market value of the underlying common stock at the date of grant. The following table summarizes the pro forma consolidated results of operations of Newtek as though the fair value based accounting method in SFAS 148 Accounting for Stock-based Compensation Transition and Disclosure an amendment of SFAS 123 had been used in accounting for stock options.

**Table of Contents****NOTE 1 SIGNIFICANT ACCOUNTING POLICIES: (Continued)**

	Stock Compensation		Stock Compensation	
	for the three months ended		for the nine months ended	
	September 30,		September 30,	
	2003	2002	2003	2002
As reported				
Net income	\$ 9,474,292	\$ 5,453,038	\$ 14,039,474	\$ 5,013,581
Deduct: Total stock based employee Compensation expense determined under fair value based method for all awards, net of related tax effects	(217,945)	(256,659)	(646,065)	(703,860)
Pro forma net income	\$ 9,256,347	\$ 5,196,379	\$ 13,393,409	\$ 4,309,721
Earnings per share:				
Basic as reported	\$ 0.37	\$ 0.22	\$ 0.55	\$ 0.21
Basic pro forma	\$ 0.36	\$ 0.21	\$ 0.52	\$ 0.18
Diluted as reported	\$ 0.36	\$ 0.22	\$ 0.54	\$ 0.21
Diluted pro forma	\$ 0.35	\$ 0.21	\$ 0.51	\$ 0.18

For 2003 and 2002, the weighted average fair value of each option granted is estimated on the date of grant using the Black Scholes model with the following assumptions: expected volatility of 60-85%, risk-free interest rate of 1.61% to 6.15%, respectively, expected dividends of \$0 and expected terms of 1-6 years.

**NOTE 2 COMMON STOCK**

In the third quarter of 2003, Newtek sold 16,666 shares of common stock in private transactions, with gross and net cash proceeds totaling \$75,000. During the same period there were approximately 37,000 stock options exercised, with gross cash proceeds totaling approximately \$108,000. In addition, 2,000 shares of common stock were issued in consideration for consulting services rendered, valued at approximately \$12,000.

During the third quarter of 2003, in connection with two employment agreements, shares of restricted stock, valued at approximately \$120,000 were issued as part of total compensation. The shares vest over a one year period. Total compensation expense for the third quarter was approximately \$22,000.

**NOTE 3 INVESTMENTS IN QUALIFIED BUSINESSES**



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The various interests that Newtek acquires in its investments are accounted for under three methods: consolidation, equity method and cost method. The applicable accounting method is generally determined based on the Company's voting interest in an investee.

**Consolidation Method.** Investments in which Newtek directly or indirectly owns more than 50% of the outstanding voting securities or those Newtek has effective control over are generally accounted for under the consolidation method of accounting and are referred to here as Partner Companies. Under this method, an investment's financial position and results of operations are reflected within the Company's Balance Sheet and Consolidated Statements of Income. All significant inter-company accounts and transactions including returns of principal, dividends, interest received and investment redemptions have been eliminated. The results of operations and cash flows of a consolidated Partner Company are included through the latest interim period in which Newtek owned a greater than 50% direct or indirect voting interest for the entire interim period or otherwise exercised control over the Partner Company. Upon dilution of control below 50%, the accounting method is adjusted to the equity or cost method of accounting, as appropriate, for subsequent periods.

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**NOTE 3 INVESTMENTS IN QUALIFIED BUSINESSES: (Continued)**

Equity Method. Investees that are not consolidated, but over which Newtek exercises significant influence, are accounted for under the equity method of accounting. Whether or not Newtek exercises significant influence with respect to an investee depends on an evaluation of several factors including, among others, representation on the Company's Board of Directors and ownership level, which is generally a 20% to 50% interest in the voting securities of the Company, including voting rights associated with the Company's holdings in common, preferred and other convertible instruments in the investee. Under the equity method of accounting, an investee's accounts are not reflected within the Company's Consolidated Balance Sheet and Consolidated Statements of Income; however, the Company's share of the earnings or losses of the investee is reflected in the caption "Equity in net losses of affiliates" in the Consolidated Statements of Income.

Cost Method. Investees not accounted for under the consolidation or the equity method of accounting are accounted for under the cost method of accounting. Under this method, the Company's share of the earnings or losses of such companies is not included in the Consolidated Balance Sheet and Consolidated Statements of Income. However, cost method impairment charges are recognized, as necessary, in the Consolidated Statement of Income. If circumstances suggest that the value of the investee has subsequently recovered, such recovery is not recorded until realized. In some of the entities which we account for under the cost or equity method, Newtek may own warrants that if exercised, would cause Newtek to use either the equity or consolidation method. As of December 31, 2002, Newtek does not expect these warrants to be exercised in the near future.

During the nine month period ended September 30, 2003, Newtek determined that there was an approximately \$943,000 of an other than temporary decline in the value of its investments for Merchant Data Systems, Inc., \$500,000 for 1-800 Gift Certificate, \$271,000 for Direct Creations, LLC \$145,000 for O.S. Johnson, LLC, \$112,000 for Gerace Auto Parts, LLC, and \$20,000 of an other than temporary decline in the value of its investments for Transworld Business Brokers, LLC. These items aggregated approximately \$1,991,000 which is shown on the statement of income as other than temporary decline in value of investments.

During the nine month period ended September 30, 2002, Newtek determined that there was approximately \$734,000 of an other than temporary decline in the value of its investments for Starphire Technologies, LLC, approximately \$77,000 other than temporary decline in the value of its investments for Embosser's Sales and Service, \$100,000 for O.S. Johnson, LLC, \$458,000 other than temporary decline in the value of its investments for Direct Creations, LLC, and an approximate \$87,000 of an other than temporary decline in the value of its investments for Gino's Seafood. In addition, Newtek determined an impairment existed for a non-Capco investment (included in prepaid expenses and other assets on the balance sheet), and recorded a charge of approximately \$162,000. In 2002, Newtek also recovered approximately \$29,000 of cash on two of its investments written down in 2000. These items aggregate approximately \$1,589,000 which is shown on the statement of income as other than temporary decline in value of investments.

The following table is a summary of such investments as of September 30, 2003, shown separately between their debt and equity components, and all terms of each are summarized. There are no expiration dates on any of the financial instruments, unless disclosed.

In accordance with the provisions of Statement of Financial Accounting Standards No. 115 "Accounting for Certain Investment in Debt and Equity Securities", Newtek classifies its debt investments as held-to-maturity and such investments are initially recorded at amortized cost. On a monthly basis, the Company's Investment Committee meets to evaluate the Company's investments. Newtek considers several factors in determining whether an impairment exists on the investment, such as the investee's net book value, cash flow, revenue growth and net income. In addition, the Investment Committee considers other factors, such as the economy and the investee company's industry, to determine if an other than temporary decline in value exists in the Company's investment



**Table of Contents****NOTE 3 INVESTMENTS IN QUALIFIED BUSINESSES: (Continued)****DEBT INVESTMENTS**

Investee	Direct Creations, LLC	Merchant Data Systems, Inc.	4G s Truck Renting	Transworld Business Brokers, LLC	Autotask Group	Louisiana BIDCO Debt Investments	Gulf Coast Bidco	Total
Investment Date (s)	Sep-01, Nov-01	Aug-00	Nov-99, Jul-00, Jun-02	Jun-01	Oct-02	Various	Dec-02	
Maturity Date	Jun-04	May-04	Aug-03	Jun-04	Sep-03	Various	Various	
Interest Rate	LIBOR	0.00%	7.40%	5.00%	7.75%	Prime +1%	Various	
Principal outstanding at December 31, 2002	\$ 373,233	\$ 942,591	\$ 100,000	\$ 140,000	\$ 200,000	\$ 1,234,029	\$ 972,500	\$ 3,962,353
Return of principal 2003	(61,923)		(100,000)	(25,000)	(200,000)	(82,932)		(469,855)
Investments in 2003					300,000			300,000
Other than temporary decline in value of its investments		(942,591)				(257,339)		(1,199,930)
Principal outstanding at September 30, 2003	\$ 311,310			\$ 115,000	\$ 300,000	\$ 893,758	\$ 972,500	\$ 2,592,568

**EQUITY INVESTMENTS**

Investee	Direct Creations, LLC	1-800 Gift Certificates, LLC	Distribution Video and Audio	BuySeasons, Inc.	Newtek Financial Info Services of LA, LLC	Transworld Business Brokers, LLC	Total
Investment Date(s)	Dec-00, Aug-02	Jul-99 Jul-01	Jun-00	Jun-01	Dec-02	Jun-01	
Type of Investment	Warrants	Common Stock/	Common Stock	Common Stock	Preferred Member	Preferred Membership	

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Warrants

Ownership Interest as of September 30, 2003	3.84%	<5%	<5%	<5%	49%	33%	
Total equity investments at December 31, 2002	\$ 270,823	\$ 500,000	\$ 200,000	\$ 100,000		\$ 20,287	\$ 1,091,110
Investments in 2003					710,000		710,000
Reclassification of consolidated investment					272,627		272,627
Equity in losses 2003					(117,904)		(117,904)
Reversal of equity in loss due to consolidation as a result of FIN 46 adoption					117,904		117,904
Reclassification to consolidated based on FIN 46 adoption					(982,627)		(982,627)
Other than temporary decline in value of its investments	(270,823)	(500,000)				(20,287)	(791,110)
Total equity investments at September 30, 2003	\$	\$	\$ 200,000	\$ 100,000	\$	\$	\$ 300,000

**Table of Contents****NOTE 3 INVESTMENTS IN QUALIFIED BUSINESSES: (Continued)**

Newtek has not guaranteed any obligation of these investees, and Newtek is not otherwise committed to provide further financial support for the investees. However, from time-to-time, Newtek may decide to provide such additional financial support which, as of September 30, 2003, was not significant. Should Newtek determine that an impairment exists upon its periodic review, and it is deemed to be other than temporary, Newtek will write down the recorded value of the asset to its estimated fair value and record a corresponding charge in the Statement of Income.

**CONSOLIDATED DEBT INVESTMENTS**

Investee	Newtek Merchant Solutions of NY, LLC	Newtek Merchant Solutions of WI, LLC	PPM Link, LLC	Newtek Business Exchange of NY, LLC	Newtek Financial Info Services of FL, LLC	DC Media Capital, LLC	Newtek Strategies - CO, LLC	Total
Investment Date(s)	Mar-01	Jun-01 Mar-03	Mar-01	Mar-02	Nov-99	Oct-02	Jun-03	
Maturity Date	Nov-05	Jun-06 Mar-08	Sep-02	Mar-05	Nov-01	Oct-03	April-04	
Interest Rate	6.00%	5.00-8.00%	5.75%	2.50%	5.25%	12.00%	3%	
Total consolidated debt investments as of December 31, 2002	\$ 685,000	\$ 1,505,000	\$ 1,000,000	\$ 325,000	\$ 150,000	\$ 163,277	\$	\$ 3,828,277
Total consolidated debt investments made in 2003		1,000,000					300,000	\$ 1,300,000
Return of principal 2003		(363,334)	(1,000,000)			(80,083)		\$ (1,443,417)
Total consolidated debt investments as of September 30, 2003	\$ 685,000	\$ 2,141,666	\$ 0	\$ 325,000	\$ 150,000	\$ 83,194	\$ 300,000	\$ 3,684,860

**CONSOLIDATED EQUITY INVESTMENTS**

Investee	Newtek Merchant Solutions of NY, LLC	Newtek Merchant Solutions of LA, LLC	Newtek Merchant Solutions of CO, LLC	PPM Link, LLC	Wilshire Louisiana Capital Management	Newtek Strategies, LLC	Newtek Business Exchange of NY, LLC	SBA Holdings, Inc.	Automated Merchant Services, Inc.
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Investment Date(s)	Fund								
	Mar-01	Sep-01	Dec-02	Mar-01	Dec-02	Aug-01	Mar-02	Sep-02	Aug-03
Type of investment	Preferred Member	Preferred Member	Preferred Member	Preferred Member	Preferred Membership	Preferred Member	Common & Preferred Member	Preferred Stock	Preferred Stock
Ownership interest	90.00%	95.00%	95.00%	90.00%	100.00%	70.00%	93.10%	80.00%	100%
Total consolidated equity Investments 2002	\$ 125,000	\$ 1,350,000	\$ 3,308,665	\$ 1,103,333	\$ 972,500	\$ 999,950	\$ 3,102,196	\$ 2,000,000	\$
Total consolidated equity investments made in 2003									\$ 2,000,000