

Canadian Forces Central Fund

**Financial Statements
March 31, 2017**



October 27, 2017

Independent Auditor's Report

To the Non-Public Property Board

We have audited the accompanying financial statements of the Canadian Forces Central Fund, which comprise the statement of financial position as at March 31, 2017 and the statements of operations and changes in net assets and cash flows for the year then ended, and the related notes which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian accounting standards for not-for-profit organizations, and for such internal control as management determines is necessary to enable the preparation 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 Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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PwC refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.



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 present fairly, in all material respects, the financial position of the Canadian Forces Central Fund as at March 31, 2017 and the results of its operations and its cash flows for the year then ended in accordance with Canadian accounting standards for not-for-profit organizations.

PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants

Canadian Forces Central Fund

Statement of Financial Position

As at March 31, 2017

	2017	2016
	\$	\$
Assets		
Current assets		
Cash (note 4)	-	2,288,253
Accrued interest and dividend receivable	243,660	233,882
Accounts receivable (note 5)	70,689,432	67,186,378
Prepaid expenses	175,132	226,183
Current portion of project loans receivable (note 6)	1,887,492	3,439,424
	<u>72,995,716</u>	<u>73,374,120</u>
Other assets		
Project loans receivable (note 6)	38,374,730	23,226,397
Long-term investments (note 7)	177,532,440	162,563,405
Equity investments (note 8)	20,767,619	21,006,261
	<u>309,670,505</u>	<u>280,170,183</u>
Liabilities and Net Assets		
Current liabilities		
Bank overdraft (note 4)	3,509,060	-
Accounts payable and accrued liabilities (note 5)	15,246,533	13,896,720
	<u>152,310,139</u>	<u>150,446,684</u>
Trust liabilities (note 9)	171,065,732	164,343,404
	<u>138,604,773</u>	<u>115,826,779</u>
Net assets	<u>309,670,505</u>	<u>280,170,183</u>

Approved on behalf of the NPP Board



Shirley Tang-Jassemi, Chief Financial Officer

The accompanying notes are an integral part of these financial statements.

Canadian Forces Central Fund

Statement of Operations and Changes in Net Assets

For the year ended March 31, 2017

	2017 \$	2016 \$
Operating revenue		
Dividends and interest	4,583,587	4,453,427
Realized gain on sale of portfolio investments	11,080,366	4,784,234
Change in unrealized loss on portfolio investments (note 7)	(685,138)	(9,427,929)
Loan interest	944,126	795,214
Income (loss) from Queensway Corporate Campus (note 8(a))	(54,580)	265,072
Loss from Lisgar Street Property (note 8(b))	(228,354)	(912)
Gain (loss) from Michael Street Property (note 8(c))	44,292	(252,577)
Re-insurance guarantee fee (note 10)	250,000	250,000
Other	990,523	980,580
	<u>16,924,822</u>	<u>1,847,109</u>
Operating expense		
CFCF management	276,314	339,033
Interest to base/wing funds, messes and trusts	8,306,721	4,703,993
CFMWS user fees for services (note 11)	350,000	350,000
Investment services	285,598	268,006
Other	895,963	199,715
	<u>10,114,596</u>	<u>5,860,747</u>
Net operating revenue (expense) before CFCF contributions	6,810,226	(4,013,638)
CFCF contributions (note 12)	9,032,232	9,860,594
Net expense before transfer from SISIP	(2,222,006)	(13,874,232)
SISIP Financial Contribution (note 11)	25,000,000	-
Net revenue (expense) for the year	22,777,994	(13,874,232)
Net assets - Beginning of year	115,826,779	129,701,011
Net assets - End of year	<u>138,604,773</u>	<u>115,826,779</u>

The accompanying notes are an integral part of these financial statements.

Canadian Forces Central Fund

Statement of Cash Flows

For the year ended March 31, 2017

	2017	2016
	\$	\$
Cash provided by (used in)		
Operating activities		
Net revenue (expense) for the year	22,777,994	(13,874,232)
Items not affecting cash -		
Realized gain on sale of portfolio investments	(11,080,366)	(4,784,234)
Unrealized loss on portfolio investments	685,138	9,427,929
Loss (income) from Queensway Corporate Campus	54,580	(265,072)
Loss from Lisgar Street Property	228,354	912
Loss (income) from Michael Street Property	(44,292)	252,577
Net change in operating components of working capital -		
Accrued interest and dividend receivable	(9,778)	(25,142)
Accounts receivable	(3,503,054)	2,956,414
Prepaid expenses	51,051	(75,090)
Accounts payable and accrued liabilities	1,349,813	4,874,418
Trust liabilities	1,863,455	4,795,955
	<u>12,372,895</u>	<u>3,284,435</u>
Investing activities		
Purchase of Michael Street Property	-	(4,499,922)
Net issuance of project loans receivable	(13,596,401)	(1,218,103)
Net purchases of portfolio investments	(4,573,807)	(4,433,610)
	<u>(18,170,208)</u>	<u>(10,151,635)</u>
Net change in cash for the year	(5,797,313)	(6,867,200)
Cash - Beginning of year	<u>2,288,253</u>	<u>9,155,453</u>
Cash (bank indebtedness) - End of year	<u>(3,509,060)</u>	<u>2,288,253</u>

The accompanying notes are an integral part of these financial statements.

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

1 Nature of operations

The Canadian Forces Central Fund (CFCF) was established by the Chief of the Defence Staff (CDS) on February 1, 1968, under Section 2 and Sections 38 to 41 of the *National Defence Act*, to provide banking services to units and trusts from non-public funds and financial assistance to units in establishing and improving messes, recreational and social facilities for the benefit of Canadian Forces personnel and their dependants. Responsibility for directing the affairs of CFCF rests with the Director General Morale and Welfare Services as delegated by the CDS.

In common with other non-public funds, CFCF is exempt from paying income tax under Part 1 of the *Income Tax Act*.

A significant portion of the transactions in these financial statements relate to military base activities.

2 Summary of significant accounting policies

Basis of accounting

These financial statements have been prepared in accordance with Canadian accounting standards for not-for-profit organizations (note 1).

Cash and cash equivalents

Cash and cash equivalents consist of balances with banks, short-term investments and cash at the brokers' account.

Financial instruments

Measurement of financial instruments

CFCF initially measures its portfolio investments at fair value. The fair value of portfolio investments is determined by reference to published price quotations in an active market at year-end. Changes in fair value are recognized in the statement of operations and changes in net assets in the year incurred.

Investments in Queensway Corporate Campus (QCC), Lisgar Street Property and Michael Street Property are accounted for under the equity method.

All other financial assets and liabilities are subsequently measured at amortized cost.

Transaction costs

Transaction costs are recognized in the statement of operations and changes in net assets in the year incurred, except for financial instruments that will be subsequently measured at amortized cost.

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

Revenue recognition

Dividends and interest are recognized when received or receivable if the amount to be received can be reasonably estimated and collection is reasonably assured.

Use of estimates

The preparation of financial statements in conformity with Canadian accounting standards for not-for-profit organizations requires management to make 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 revenue and expense during the reporting period.

Management makes estimates in determining the estimated net realizable value of accounts receivable, project loans receivable and the amount of accrued liabilities. Actual results could differ from those estimates. These estimates are reviewed annually and as adjustments become necessary, they are recognized in the financial statements in the period they become known.

3 Financial instruments and risk management

CFCF is exposed to various risks through its financial instruments. The following analysis provides a measure of CFCF's risk exposure and concentrations.

CFCF does not use derivative financial instruments to manage its risks.

Credit risk

Credit risk arises principally from cash and cash equivalents, accrued interest receivable, accounts receivable, project loans receivable and long-term investments. CFCF generally places its cash and cash equivalents in Canadian federal and provincial government bonds, bonds of corporations with high credit ratings and bankers' acceptances.

CFCF does not require collateral or other security to support project loans advanced to military bases and ships and therefore, these loans bear an element of credit risk. However, losses due to amounts proving uncollectible have traditionally been low due in part to the fact that CFCF administers the cash balances of most of its creditors.

Liquidity risk

Liquidity risk refers to the adverse consequences that CFCF will encounter difficulty in meeting obligations associated with financial liabilities, which are comprised of accounts payable and employee deductions payable.

CFCF manages this risk by maintaining sufficient cash and cash equivalents to meet their current obligations and management establishes budget and cash estimates to determine their future cash flow requirements. CFCF has an operating credit facility of \$10 million which bears interest at the bank's prime rate plus 0.50%.

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk is comprised of currency risk, interest rate risk and other price risk.

Currency risk

Currency risk refers to the risk that the fair value of financial instruments or future cash flows associated with the instruments will fluctuate relative to the Canadian dollar due to changes in foreign exchange rates.

CFCF's exposure to foreign currency risk is primarily related to fluctuations in the value of the Canadian dollar relative to that of the US dollar. As at March 31, 2017, approximately \$23.5 million of CFCF's long-term investments are exposed to fluctuations in the US dollar.

Interest rate risk

Interest rate risk refers to the risk that the fair value of financial instruments or future cash flows associated with the instruments will fluctuate due to changes in market interest rates.

Exposure to interest rate risk on long-term investments is disclosed in note 7. CFCF pays interest on net trust liabilities to the units and funds based on the bank's prime rate or CFCF's investment rate of return.

Other price risk

Other price risk refers to the risk that the fair value of financial instruments or future cash flows associated with the instruments will fluctuate because of changes in market prices (other than those arising from currency risk or interest rate risk), whether those changes are caused by factors specific to the individual instrument or its issuer or factors affecting all similar instruments traded in the market.

Other price risk affecting long-term investments is disclosed in note 7.

Changes in risk

There have been no material changes in CFCF's risk exposures from the prior year.

4 Consolidated bank account

CFCF maintains cash in its consolidated bank account on behalf of other funds, trusts and units. The interest earned on such funds is recorded as revenue of CFCF. CFCF pays the respective funds, trusts and units for cash managed on their behalf. Base/Wing/Funds and Messes receive either 3%, the bank's prime rate plus 0.25%, or CFCF's investment rate of return less 0.5% for its cash balance in excess of CFCF liabilities while trust accounts receive varying percentages based on cash balances and options selected. These amounts are recorded as interest expense in the statement of operations and changes in net assets.

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

5 Accounts receivable and accounts payable and accrued liabilities

As part of the Non-Public Property Board approved Customer Relationship Management Project, CFCF assumes and manages the accounts receivable and accounts payable and accrued liabilities of all activities undertaken by Canadian Forces Morale and Welfare Services (CFMWS), Base/Wing/Unit Funds, the Canadian Forces Exchange System (CANEX), Specialty Interest Activities and Messes.

Accounts receivable are comprised of the following:

	2017 \$	2016 \$
CANEX	61,427,060	60,851,108
CFMWS	128,945	949,573
Base/Wing/Funds/Messes	4,494,766	5,612,567
	<u>66,050,771</u>	<u>67,413,248</u>
Trade and other receivables	5,168,438	302,907
	<u>71,219,209</u>	<u>67,716,155</u>
Less: Allowance for doubtful accounts	<u>529,777</u>	<u>529,777</u>
	<u>70,689,432</u>	<u>67,186,378</u>

In regards to the accounts receivable that are assumed on behalf of CANEX, approximately \$58.7 million (2016 - approximately \$57.6 million) relates to CANEX's interest free credit plans that are available for eligible patrons with the balance of the accounts receivable being for trade receivables. There are varying repayment terms in regards to the CANEX credit plans ranging from one-year to three-year plans.

Included in receivable at March 31, 2017, are government remittances owing of \$61,736 (2016 - \$nil).

Accounts payable and accrued liabilities are comprised of the following:

	2017 \$	2016 \$
CANEX	5,710,957	7,462,151
CFMWS	1,797,911	6,013,759
Base/Wing/Funds/Messes	4,629,444	3,434,837
	<u>12,138,312</u>	<u>16,910,747</u>
Trade and other	3,108,221	(3,014,027)
	<u>15,246,533</u>	<u>13,896,720</u>

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

Included in accounts payable and accrued liabilities at March 31, 2017, are government remittances owing of \$nil (2016 - \$843,484).

6 Project loans receivable

CFCF provides unsecured loans to military bases and ships to share in the financing of capital projects. CFCF provides interest free working capital loans to units on deployed operations for the duration of the deployment. Starting in May 2002, ships may obtain a line of credit on their Consolidated Bank Account when being deployed on various operations instead of an interest free loan. Loans to CANEX and to bases bear interest at 4%. Repayment terms vary from 3 to 20 years. Periodically, the Non-Public Property Board approves the full or partial forgiveness of specific loan balances. No loans were forgiven in either the 2017 or 2016 fiscal years.

	2017 \$	2016 \$
Interest bearing loans	24,099,447	22,253,271
Interest-free loans	16,162,775	4,412,550
	<u>40,262,222</u>	<u>26,665,821</u>
Less: Current portion	1,887,492	3,439,424
	<u>38,374,730</u>	<u>23,226,397</u>

7 Long-term investments

	2017 Market value \$	2017 Cost \$	2016 Market value \$	2016 Cost \$
Portfolio investments				
Cash and cash equivalents	2,009,870	2,009,870	2,222,396	2,222,396
Canadian stocks	51,563,746	41,631,915	50,265,187	44,401,945
International stocks	57,540,291	45,246,619	49,702,415	35,995,110
Canadian bond fund	66,418,533	67,526,524	60,373,407	58,141,304
	<u>177,532,440</u>	<u>156,414,928</u>	<u>162,563,405</u>	<u>140,760,755</u>

Portfolio investments are managed by external investment managers who are under the direction of the Investment Committee reporting to the Non-Public Property Board.

a) Interest rate risk

The organization manages its interest rate risk exposure through its investment in the aforementioned Canadian bond fund. This fund minimizes its interest rate risk by using a laddered portfolio with varying terms to maturity. The laddered structure of maturity helps to enhance the average portfolio yield while reducing the sensitivity of the portfolio to the impact of interest rate fluctuations.

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

b) Credit and market risk

Risk and volatility of investment returns are mitigated through the diversification of investments in different business sectors and corporation sizes.

8 Equity investments

	2017 \$	2016 \$
Equity in Queensway Corporate Campus	15,044,068	15,098,648
Equity in Lisgar Street Property	1,431,974	1,660,329
Equity in Michael Street Property	4,291,577	4,247,284
	<u>20,767,619</u>	<u>21,006,261</u>

a) Equity in Queensway Corporate Campus

The Queensway Corporate Campus (QCC) is accounted for under the equity method. The QCC was acquired by CFCF on December 24, 2009, for \$56.8 million with \$18 million provided at the time of the purchase and the balance of \$38.8 million financed through long-term debt. This campus encompasses the real estate located at 4200 Labelle Street, 4210 Labelle Street and 1223 Michael Street.

The equity in QCC as at March 31 is presented below.

Statement of net assets of QCC as at March 31 is as follows:

	2017 \$	2016 \$
Total assets	48,165,540	48,906,574
Total liabilities	<u>33,121,472</u>	<u>33,807,926</u>
Net assets	<u>15,044,068</u>	<u>15,098,648</u>

Statement of operations of QCC for the year ended March 31 is as follows:

	2017 \$	2016 \$
Rental revenue	9,302,836	9,560,339
Rental expenses	<u>9,357,416</u>	<u>9,295,267</u>
Net income (loss) for the year	<u>(54,580)</u>	<u>265,072</u>

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

Cash flows of QCC for the year ended March 31 is as follows:

	2017 \$	2016 \$
Cash flows from operating activities	2,008,507	2,591,000
Cash flows from investing activities	(2,226)	-
Cash flows from financing activities	(901,929)	(4,171,432)
	<u>1,104,352</u>	<u>(1,580,432)</u>

b) Equity in Lisgar Street Property

Lisgar Street Property is accounted for under the equity method. The Lisgar Street Property was acquired by CFCF on October 3, 2014, for \$1.7 million. This property is located at 66 Lisgar Street in Ottawa.

The equity in Lisgar Street Property as at March 31 is presented below.

Statement of net assets of Lisgar Street Property as at March 31 is as follows:

	2017 \$	2016 \$
Total assets	1,443,871	1,695,824
Total liabilities	11,897	35,495
Net assets	<u>1,431,974</u>	<u>1,660,329</u>

Statement of operations of Lisgar Street Property for the year ended March 31 is as follows:

	2017 \$	2016 \$
Rental revenue	42,128	130,822
Rental expenses	270,482	131,734
Net loss for the year	<u>(228,354)</u>	<u>(912)</u>

Cash flows of Lisgar Street Property for the year ended March 31 is as follows:

	2017 \$	2016 \$
Cash flows from operating activities	<u>(228,354)</u>	<u>(912)</u>

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

On June 20, 2017, CFCF finalized the sale of the Lisgar Street Property for \$1,200,000. The sale price reflects the net book value of the property as of March 31, 2017, after impairments of \$127,358 were applied in fiscal year 2017.

c) Equity in Michael Street Property

Michael Street Property is accounted for under the equity method. The Michael Street Property was acquired by CFCF on September 1, 2015, for \$4.5 million. This property is located at 1209 Michael Street in Ottawa.

The equity in Michael Street Property as at March 31 is presented below.

Statement of net assets of Michael Street Property as at March 31 is as follows:

	2017	2016
	\$	\$
Total assets	4,452,759	4,264,666
Total liabilities	161,182	17,382
Net assets	4,291,577	4,247,284

Statement of operations of Michael Street Property for the year ended March 31 is as follows:

	2017	2016
	\$	\$
Rental revenue	623,094	-
Rental expenses	578,802	252,577
Net income (loss) for the year	44,292	(252,577)

Cash flows of Michael Street Property for the year ended March 31 is as follows:

	2017	2016
	\$	\$
Cash flows from operating activities	44,292	(252,577)

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

9 Trust liabilities

CFCF maintains assets in trust on behalf of the following entities:

	2017 \$	2016 \$
Base funds, messes and others	98,184,099	104,503,789
CANEX	29,544,434	26,155,052
CFMWS	(14,878,418)	(16,318,107)
SOT	17,511,547	15,032,118
Regimental funds and alike	14,618,568	13,749,651
NPF Pension/Benefits	3,820,798	3,273,033
QCC/Lisgar/Michael	3,305,879	3,462,585
SISIP	203,232	588,563
	<u>152,310,139</u>	<u>150,446,684</u>

10 Re-insurance guarantee fee

CFCF is contingently liable to a maximum of \$100 million as part of the SISIP re-insurance coverage for Canadian wartime efforts with the annual fee being calculated at 0.25% of the amount guaranteed. This fee has been recorded at its carrying amount which is the amount agreed to by management of both organizations.

11 Related party transactions

Non-Public Property (NPP), as defined under the *National Defence Act*, consists of money and property contributed by Canadian Forces members and is administered for their benefit by the Canadian Forces Morale and Welfare Services (CFMWS). The CFMWS is responsible for delivering selected morale and welfare programs, services and activities through two operational divisions, Personnel Support Programs and Commercial Services (CANEX and SISIP Financial Services).

Under the *National Defence Act*, NPP is explicitly excluded from the *Financial Administration Act*. The government provides some services to NPP such as accommodation and security for which no charge is made. The cost of providing these services is included in the Public Accounts.

NPP estimated revenue and expense of approximately \$420 million and \$396 million for the year ended March 31, 2017, respectively, and net equity of \$761 million at March 31, 2017, are excluded from the financial statements of the Government of Canada.

During the year, there was a charge to CFCF by CFMWS in the amount of \$350,000 (2016 - \$350,000) for accounting services provided by CFMWS. These transactions are in the normal course of operations and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

During the year, in addition to its annual support SISIP contributed an additional \$25,000,000 to CFCF to support NPP programs, capital and operations and maintenance projects.

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2017

12 CFCF contributions

During the year, \$9,032,232 (2016 - \$9,860,594) was provided by CFCF to CFMWS, representing financial support provided for the NPF wide services of accounting, human resources management, information management and information technology and consolidated insurance programs as well as the corporate operating costs.

13 Contingent liabilities

CFCF is contingently liable for \$44,000 (2016 - \$44,000) for letters of credit supplied to various provincial liquor boards on behalf of unit messes.

CFCF, along with CANEX and SISIP, has also provided a letter of acknowledgement to the Bank of Montreal to fund any shortfall in the long-term debt payments to be made by QCC. At March 31, 2017, this long-term debt of QCC amounted to \$32,229,809 (2016 - \$33,291,774) (note 8).