

Canadian Forces Non-Public Funds Employees Pension Plan

Financial Statements
December 31, 2016

Assets	Liabilities	Net Assets
<p>Investments in public securities</p> <p>Investments in private securities</p> <p>Real estate</p> <p>Other investments</p> <p>Accounts receivable</p> <p>Prepaid expenses</p> <p>Other assets</p>	<p>Accounts payable</p> <p>Accrued liabilities</p> <p>Other liabilities</p>	<p>Net investments</p> <p>Other net assets</p>

Income Statement	Balance Sheet
<p>Investment income</p> <p>Real estate income</p> <p>Other income</p> <p>Expenses</p>	<p>Assets</p> <p>Liabilities</p> <p>Net Assets</p>



June 28, 2017

Independent Auditor's Report

To the Non-Public Property Board of Canadian Forces Non-Public Funds Employees Pension Plan

We have audited the accompanying financial statements of Canadian Forces Non-Public Funds Employees Pension Plan, which comprise the statement of financial position as at December 31, 2016 and the statements of changes in net assets available for benefits, changes in accrued pension benefits and changes in surplus 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 pension plans 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 Non-Public Funds Employees Pension Plan as at December 31, 2016 and the changes in net assets available for benefits, surplus and changes in accrued pension benefits for the year then ended in accordance with Canadian accounting standards for pension plans.

PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants

Canadian Forces Non-Public Funds Employees Pension Plan

Statement of Financial Position

As at December 31, 2016

	2016 \$	2015 \$
Net Assets Available for Benefits		
Assets		
Cash (note 3)	1,694,796	-
Investments (notes 3 and 5)	317,170,599	283,625,113
Due from Canadian Forces Central Fund (note 6)	2,226,791	4,600,639
	<u>321,092,186</u>	<u>288,225,752</u>
Liabilities		
Plan expenses payable (note 7)	1,261,444	672,039
Due to broker	1,694,796	-
	<u>2,956,240</u>	<u>672,039</u>
Net assets available for benefits	<u>318,135,946</u>	<u>287,553,713</u>
Accrued Pension Benefits and Surplus		
Actuarial value of accrued pension benefits (note 8)	243,028,000	229,948,000
Surplus (note 8)	75,107,946	57,605,713
	<u>318,135,946</u>	<u>287,553,713</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 Non-Public Funds Employees Pension Plan
Statement of Changes in Net Assets Available for Benefits
For the year ended December 31, 2016

	2016	2015
	\$	\$
Increase in assets		
Contributions -		
Employer - Regular	9,547,890	8,188,421
Employer - Special	5,928,250	7,931,842
Employee	4,807,477	4,597,617
Changes in fair value of investments	9,437,380	1,638,135
Distribution income	13,799,024	11,267,230
Interest income	79,507	60,825
Total increase in assets	43,599,528	33,684,070
Decrease in assets		
Annuity payments	7,865,822	7,171,594
Termination benefits	3,877,553	4,474,393
Investment management fees	1,273,920	1,312,935
Total decrease in assets	13,017,295	12,958,922
Increase in net assets	30,582,233	20,725,148
Net assets available for benefits - Beginning of year	287,553,713	266,828,565
Net assets available for benefits - End of year	318,135,946	287,553,713

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

Canadian Forces Non-Public Funds Employees Pension Plan

Statement of Changes in Accrued Pension Benefits

For the year ended December 31, 2016

	2016 \$	2015 \$
Increase in benefits		
Interest accrued on benefits	13,531,586	12,353,890
Benefits accrued	14,465,699	12,877,924
Adjustment to valuation of accrued pension benefits	-	7,590,173
	<hr/>	<hr/>
Increase in accrued benefits	27,997,285	32,821,987
Decrease in accrued benefits		
Annuity payments and refunds	11,743,375	11,645,987
Adjustment to valuation of accrued pension benefits	3,173,910	-
	<hr/>	<hr/>
Decrease in accrued benefits	14,917,285	11,645,987
Net increase in accrued pension benefits	13,080,000	21,176,000
Accrued pension benefits - Beginning of year	<hr/>	<hr/>
	229,948,000	208,772,000
Accrued pension benefits - End of year	<hr/>	<hr/>
	243,028,000	229,948,000

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

Canadian Forces Non-Public Funds Employees Pension Plan
Statement of Changes in Surplus
For the year ended December 31, 2016

	2016 \$	2015 \$
Surplus of net assets available for benefits versus accrued benefits - Beginning of year	57,605,713	58,056,565
Net increase in net assets available for benefits	30,582,233	20,725,148
Net increase in accrued pension benefits	<u>(13,080,000)</u>	<u>(21,176,000)</u>
Surplus of net assets available for benefits versus accrued benefits - End of year	<u>75,107,946</u>	<u>57,605,713</u>

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

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

1 Description of pension plan

The Canadian Forces Non-Public Funds Employees Pension Plan ("the Plan") became effective January 1, 1969 and was established under the provisions of Section 38 of the *National Defence Act* to account for the accumulation of employee deductions and employer contributions from participating bases, the transfer of such funds to the custodian for investment purposes and the recording of fund assets and liabilities. The Plan's trustee is Manulife Financial, its fund managers are Manulife Financial, Russell Investments and Bentall Kennedy, and its actuary is Mercer (Canada) Limited. The Plan's registration number with the Office of the Superintendent of Financial Institutions (OSFI) is 55228.

The Plan is a registered pension plan as defined in the *Income Tax Act* and as such, is not subject to income taxes. The Plan's registration number for income tax purposes is 0277954.

The following description of the Plan is a summary only. For more information, reference should be made to the Plan text.

General

The Plan is a contributory defined benefit plan integrated with the Canada/Quebec Pension Plan and registered under the *Pension Benefits Standards Act of Canada*. Plan membership is compulsory from the date of hire for all indeterminate full-time employees. Plan membership is compulsory for temporary full-time employees on the earlier of the day the employee accepts an offer of temporary full-time employment that results in a term of their temporary full-time employment being at least 24 months of continuous employment, or the day on which the employee completes 24 months of continuous employment as a temporary full-time employee. Part-time employees may join the Plan after two years of continuous service and two consecutive years with earnings in excess of 35% of the Year's Maximum Pensionable Earnings (YMPE).

Funding policy

The Plan is funded by the plan members (employees) and the sponsor (employer).

The employee contributes 4.5% of earnings which are not in excess of the Canada/Quebec Pension Plan YMPE and 6% of the member's earnings in excess of the YMPE. Members cease making contributions when they reach 35 years of service.

The employer contributes actuarially recommended amounts sufficient to satisfy any experience deficiency and provide pension benefits accruing to plan members during the current year using the previous year actuarial valuation. The most recent actuarial valuation of the Plan was as at December 31, 2016.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

Service pension

Employees meeting eligibility conditions are entitled to annual pension benefits beginning at age 65 for service on or after January 1, 1997, equal to 1.5% of the employees' average pensionable earnings up to the average YMPE plus 2% of the employees' average pensionable earnings above the average YMPE times the number of years of pensionable service since January 1, 1997 plus, for service before January 1, 1997, the greater of:

- a) 40% of the employees' total required contributions before January 1, 1997;
- b) 1.5% of the employees' average pensionable earnings up to the average YMPE plus 2% of the employees' average pensionable earnings above the average YMPE times the years of pensionable service before January 1, 1997; or
- c) 1.8% of the employees' average annualized earnings for 1994, 1995 and 1996 up to \$34,900 plus 2.4% of the employees' average annualized earnings for 1994, 1995 and 1996 above \$34,900 but below \$52,350 plus 2% of the employees' average annualized earnings for 1994, 1995 and 1996 above \$52,350 times the number of years of pensionable service before January 1, 1997.

Employees with less than three years of pensionable service are only eligible for the greater of a) or b) for their service prior to January 1, 1997. Pensions in payment have been indexed on an adhoc basis at a rate of 75% of the consumer price index. The most recent adjustment was effective September 1, 2007.

Pensionable earnings means base salary and wages including overtime, performance and incentive pay, pay during working notice period, acting pay, paid leave, vacation payouts, commissions, and other recurring categories of pay as designated by the employer, but excluding bonuses, special remunerations and gratuities. Average pensionable earnings mean the employee's average earnings as a plan member during the three highest paid consecutive years of pensionable service in the 10 years preceding the date on which pensionable service ceases to accrue.

Employees who have ten or more years of pensionable service may retire at age 60 and receive an immediate unreduced pension. Employees who are at age 50 with 10 or more years of pensionable service may elect to retire early and receive a pension reduced by 0.25% for each month that the actual retirement date precedes their 60th birthday. Employees who are at age 55 with less than 10 years of pensionable service may elect to retire early and receive a pension reduced by 0.25% for each month that the actual retirement date precedes their 65th birthday.

The Chief Executive Officer approved an initiative to give the Canadian Forces Non-Public Funds full-time and part-time employees the opportunity to buy back pensionable services during the previously imposed mandatory or the voluntary waiting periods. The pension buy back commenced in year 2004. For the previously imposed mandatory periods, the buy-back cost was shared between the employee and the employer and for the voluntary waiting periods, the employee was fully responsible for the cost.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

Bridge benefits

An employee who retires early from active service and who satisfies the eligibility requirements as follows.

- a) Has attained age 55 at retirement;
- b) Must have completed at least five years of pensionable services at retirement; and,
- c) The sum of the employees' age and completed years of pensionable service at retirement must be equal to at least 65.

Employees who meet eligibility are entitled to receive an annual bridge benefit payable in equal monthly instalments in an amount equal to \$15 per month for each completed year and partial year of pensionable service, to a maximum of 20 years. Such bridge benefit is payable from the date that the early retirement pension commences and ceases with the payment for the month of the employee's normal retirement date or in case of death, prior to normal retirement date, effective the month following the death of the employee.

Death benefits

The normal form of pension provides for monthly payments for the life of retired members with 180 payments guaranteed. Should the employee die before receiving the guaranteed 180 monthly payments, the value of the remaining payments will be paid to the beneficiary in a lump sum. If the employee has a spouse at retirement, the automatic option provides that a joint pension in an amount that is the actuarial equivalent of the normal form is payable throughout the joint lifetime of the employee and spouse, reducing to 60% on the death of the employee. An employee may elect a joint and survivor pension which provides for a benefit of 100% to the surviving spouse after death. In the event the normal form is not the form payable, the benefit payable will be the actuarial equivalent of the normal form, which cannot exceed the amount payable under the normal form.

If death occurs before becoming eligible for early retirement, the member's surviving spouse, or if there is no surviving spouse, the beneficiary, or if no beneficiary exists, the member's estate, is entitled to a death benefit. The amount of the death benefit is equal to the transfer value to which the member would have been entitled if employment had terminated on the date of death. The surviving spouse, if any, may elect among the following alternatives: transfer to a locked in Registered Retirement Savings Plan (RRSP), transfer to a registered pension plan or purchase an immediate life annuity or deferred life annuity. The beneficiary or the member's estate shall receive the death benefit in a cash lump sum, less withholding taxes.

Notwithstanding the above, if the death benefit is less than 20% of the YMPE in the calendar year of the member's death, the surviving spouse may elect to transfer the death benefit in accordance with the alternatives listed above without a locked in requirement, or may receive the death benefit in a cash lump sum payment less withholding taxes.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

If a member dies after becoming eligible for early retirement, the surviving spouse is entitled to an annuity payable for life. The amount of the annuity shall be determined as if the member had actually retired on the date of the member's death and had elected the automatic option. Where there is no surviving spouse, the beneficiary, or if there is no beneficiary, the member's estate is entitled to the value to which the member would have been entitled if employment had terminated on the date of death.

Termination benefits

A member who terminates employment is entitled to receive a pension deferred to his/her pensionable age which means the earliest age at which a member may begin to receive a pension benefit without the consent of the employer and without reduction by reason of early retirement. The member may also elect to receive a deferred pension earlier. In lieu of receiving a deferred pension, the member may elect to have the transfer value transferred to a locked in RRSP or a new employer's registered pension plan, or purchase an immediate life annuity or deferred life annuity.

However, if the transfer value of the deferred pension is less than 20% of the YMPE for the calendar year in which the termination of employment occurs, the member shall receive a lump sum cash refund of the transfer value, or may elect to transfer this amount as outlined above without a locked in requirement.

2 Summary of significant accounting policies

Basis of accounting

These financial statements have been prepared in accordance with Canadian accounting standards for pension plans. These financial statements are prepared on a going concern basis and present the information of the Plan as a separate financial reporting entity independent of the sponsor and Plan members. The Plan applies Canadian accounting standards for private enterprises in Part II of the Chartered Professional Accountants Canada (CPA) Handbook - *Accounting*, for its accounting policies not related to its investment portfolio or pension obligations.

Investments

Investment assets are recorded at fair value in accordance with IFRS 13, *Fair Value Measurement*. Purchases and sales of investments are recorded as of the trade date (the date on which the substantial risks and rewards have been transferred). Transactions that have not been settled are reflected in the statement of net assets available for benefits as amounts receivable or payable.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

Investment income

Distribution income is recorded to the extent received.

Net realized and unrealized gains and losses on investments are presented in aggregate in the statement of changes in net assets available for benefits as changes in fair value of investments, since the information to segregate the individual elements is not readily available from the Plan's trustee. All changes in fair value of investments are recorded in the statement of changes in net assets available for benefits in the year in which they occur.

Termination refunds and transfers

When a vested Plan member ceases to be employed by the sponsor, the Plan records a liability to the member on receipt of the signed election form requesting a refund or transfer of assets. The amount of the liability is determined in accordance with the actuarial calculation.

Administration expenses

Pension administration costs and professional fees are paid for by the sponsor and are accounted for as employee benefits in the year-end financial statements of the Canadian Forces Morale and Welfare Services.

Use of estimates

The preparation of financial statements requires the sponsor to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expense during the reporting period. Actual results could differ from those estimates. The most significant estimates relate to the determination of the fair value of financial instruments (note 5).

Income taxes

The Plan is a registered pension plan as defined under the *Income Tax Act* (Canada) and is not subject to income taxes in Canada.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

3 Investments

Investments as at December 31 are summarized as follows.

	2016		2015	
	Market	Book Value	Market	Book Value
	\$	\$	\$	\$
Cash	1,694,796	1,694,796	-	-
Pooled funds				
Short-term notes	9,711,409	9,711,409	5,504,394	5,534,143
Fixed income	112,068,160	116,013,549	110,174,511	112,916,513
Canadian Equities	61,323,580	60,684,163	49,946,333	59,632,290
Foreign Equities	105,586,168	97,149,704	97,642,186	90,474,761
Real estate	28,481,282	28,767,104	20,357,689	16,654,416
Total cash and investments	318,865,395	314,020,725	283,625,113	285,212,123

4 Financial risk management

The Plan's investment portfolio is subject to a variety of financial instrument risks that could adversely affect its cash flows, financial position and income. The Plan's financial risks are concentrated in its investment holdings described in the tables in note 3. These risks include credit risk, liquidity risk and market risk (including interest rate risk, currency risk and other price risk).

The Plan's Statement of Investment Policies and Procedures (SIPP) prescribes an asset mix policy, requires portfolio investment diversification, sets guidelines on investment categories, and limits exposure to individual investments and major asset classes.

The sensitivity analysis provided is hypothetical and should be used with caution as the impacts provided are not necessarily indicative of the actual impacts that would be experienced as the Plan's actual exposure to market rates may change. Changes in fair value or cash flows based on a variation in a market variable cannot be extrapolated because the relationship between the change in a market variable and the change in fair value or cash flows may not be linear. In addition, the effect of a change in a particular market variable on fair values or cash flows is calculated without considering interrelationships between the various market rates or mitigating actions that would be taken by the Plan.

Credit risk

Credit risk is the risk of loss should the counterparty to a transaction default or otherwise fail to perform under the terms of the contract. The Plan is indirectly susceptible to credit risk through its investments in pooled funds. This risk is not directly managed by the Plan.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

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Liquidity risk

Liquidity risk is the risk that the Plan will not be able to meet its financial obligations as they fall due including satisfying pension benefit payments, expenses and the ongoing requirements to satisfy its benefit obligations as discussed in note 8. The risk the Plan would be unable to meet such obligations is managed through the Plan's ongoing monitoring of the investment manager and in their ability to redeem units in the individual pooled funds in which the Plan has invested. All plan liabilities, other than pension obligations, are due and payable within ninety (90) days.

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 includes interest rate risk, currency risk and other price risk.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of the Plan's investments will fluctuate due to changes in market interest rates. It arises from the potential variation in the timing and amount of cash flow related to the Plan's assets and liabilities.

The Plan's investments consist of pooled funds which in turn invest in a diversified portfolio of assets. While the underlying investments of the pooled funds are susceptible to interest rate risk, the risk to the Plan is indirect in nature and is not directly managed by the Plan. The Plan has no direct exposure to interest risk.

Currency risk

Currency risk is the risk that the value of the Plan's investments will fluctuate due to changes in foreign exchange rates. It arises from securities that are denominated in a currency other than the Canadian dollar, which is the Plan's reporting currency.

The Plan is exposed to indirect currency risk to the extent that the pooled funds invest in financial instruments that are denominated in a currency other than the Canadian dollar.

Other price risk

Price risk is the risk that the fair value or future cash flows of financial instruments will fluctuate as a result of changes in market prices, other than those arising from foreign exchange risk or interest rate risk. The investments of the Plan are directly exposed to other price risk arising from changes in the unit prices of the pooled funds. If these unit prices were to increase or decrease by 1%, with all other variables being held constant, the impact on the net assets available for benefits would be approximately \$3,171,706 (2015-\$2,836,511).

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

5 Fair value measurement

The following is a summary of the methods used to determine the fair value of the Plan's financial instruments and an analysis of those instruments that are measured at fair value using the hierarchy set forth in the Appendix to CPA Canada Handbook - *Accounting* Section 4600. The hierarchy prioritizes the inputs to fair value measurement, placing the highest priority on unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to inputs not based on observable market data (Level 3).

The three levels of the fair value hierarchy are:

- Level 1 - unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 - inputs that are observable for the assets or liabilities either directly or indirectly; and
- Level 3 - inputs for assets or liabilities that are not based on observable market data.

The pooled funds have all been designated as Level 2 investments.

6 Due from Canadian Forces Central Fund (CFCF)

The amount due from CFCF of \$2,226,791 (2015 - \$4,600,639) represents amounts held in trust. CFCF operates under the authority of the Chief of the Defence Staff (CDS) in its Non-Public Property (NPP) capacity. Responsibility for directing the affairs of CFCF rests with the Director General Morale and Welfare Services as delegated by the CDS.

7 Plan expenses payable

Included in plan expenses payable are accrued bridge benefits payable to terminated members of the Plan between 1999 and 2013 of \$941,800. Additional payments will be made for the years 1999 to 2007 for terminated members, this amount is not yet determinable and has not been accrued.

8 Actuarial value of accrued pension benefits

Accrued pension benefits is the actuarially determined present value amount required to satisfy all future pension obligations for active and retired plan members at the statement date. An actuarial valuation of the Plan was made as at December 31, 2016, by Mercer (Canada) Limited, the Plan's actuaries.

The significant assumptions used are:

- Life expectancy of participants as per the 2014 Canadian Pensioners Mortality Table;
- 5.85% interest rate; and
- 3.25% salary escalation rate.

Canadian Forces Non-Public Funds Employees Pension Plan

Notes to Financial Statements

December 31, 2016

The purpose of the aforementioned actuarial valuation is to determine the value of the Accrued Pension Benefits as at December 31, 2016, for financial statement purposes. Based on the year-end valuation of the Accrued Pension Benefits in the amount of \$243,028,000 the Plan is in a surplus position at December 31, 2016, of \$75,107,946. In addition, the Plan was actuarially valued at December 31, 2016, on a going concern basis as well as on the solvency basis.

Under the going concern basis, this valuation compares the relationship between the value of the Plan's assets and the present value of the expected future benefit cash flows in respect of accrued service, assuming the Plan will be maintained indefinitely. Under this scenario, the valuation resulted in a surplus of \$73.4 million.

Conversely, under the hypothetical solvency (or wind up) basis, the Plan is assumed to be wound up and settled on the valuation date, assuming benefits are settled in accordance with the existing taxation rules and under circumstances producing the maximum wind up liabilities on the valuation date. This valuation resulted in a deficit of \$41.3 million.

These valuations are utilized to assess monthly and annual employer contributions. The Plan is required to have its next actuarial valuation performed as at December 31, 2017.

9 Capital management

Management of the Plan defines capital as the net assets available for benefits. The Plan's objective when managing its capital is to safeguard its ability to continue as a going concern in order to maintain adequate assets to support development of the investment activities of the Plan and to ensure adequate assets to fund future benefit payments. The Plan's policy is to invest in a diversified portfolio of investments, based on criteria established in the SIPP which assists in the management of capital and mitigation of risk.

Management monitors capital on the basis of the value of net assets available for benefits in relation to the pension obligation for funding purposes. In accordance with the requirements of the *Pension Benefits Standards Act*, the pension obligation is updated every three years or more frequently if required through an actuarial valuation process. The results of the most recent valuation have been disclosed in note 8. There has been no change in the policies with respect to management of capital in the current year.

As at December 31, 2016, all contributions that were required by that date have been remitted to the Plan.

10 Comparative figures

Certain comparative figures have been reclassified in order to conform to the current year presentation.