

Canadian Forces Central Fund

Financial Statements
March 31, 2016



January 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, 2016, 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, 2016, 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

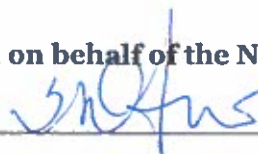
Canadian Forces Central Fund

Statement of Financial Position

As at March 31, 2016

	2016 \$	2015 \$
Assets		
Current assets		
Cash and cash equivalents (note 4)	2,288,253	9,155,453
Accrued interest receivable	233,882	208,740
Accounts receivable (note 5)	67,186,378	70,142,792
Prepaid expenses	226,183	151,093
Current portion of project loans receivable (note 6)	3,439,424	1,946,414
	<u>73,374,120</u>	<u>81,604,492</u>
Other assets		
Project loans receivable (note 6)	23,226,397	23,501,304
Long-term investments (note 7)	162,563,405	162,773,490
Equity investments (note 8)	21,006,261	16,494,756
	<u>280,170,183</u>	<u>284,374,042</u>
Liabilities and Net Assets		
Current liabilities		
Accounts payable and accrued liabilities (note 5)	13,896,720	9,022,302
Trust liabilities (note 9)		
	<u>150,446,684</u>	<u>145,650,729</u>
	164,343,404	154,673,031
Net assets		
	<u>115,826,779</u>	<u>129,701,011</u>
	<u>280,170,183</u>	<u>284,374,042</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, 2016

	2016 \$	2015 \$
Operating revenue		
Dividends and interest	4,453,427	4,831,735
Realized gain on sale of portfolio investments	4,784,234	8,838,768
Unrealized gain (loss) on portfolio investments (note 7)	(9,427,929)	9,084,840
Loan interest	795,214	977,106
Income (loss) from Queensway Corporate Campus (note 8(a))	265,072	(141,708)
Income (loss) from Lisgar Street Property (note 8(b))	(912)	1,324
Loss from Michael Street Property (note 8(c))	(252,577)	-
Re-insurance guarantee fee (note 10)	250,000	250,000
Other	980,580	869,596
	<u>1,847,109</u>	<u>24,711,661</u>
Operating expense		
CFCF management	339,033	422,638
Interest to base/wing funds, messes and trusts	4,703,993	12,113,756
CFMWS user fees for services (note 11)	350,000	350,000
Investment services	268,006	278,398
Other	199,715	249,346
	<u>5,860,747</u>	<u>13,414,138</u>
Net operating revenue (expense) before CFCF contributions	<u>(4,013,638)</u>	<u>11,297,523</u>
CFCF contributions (note 12)		
Programs and distributions	564,993	408,874
NPF services and operations	9,295,601	7,795,508
	<u>9,860,594</u>	<u>8,204,382</u>
Net revenue (expense) for the year	<u>(13,874,232)</u>	<u>3,093,141</u>
Net assets - Beginning of year	<u>129,701,011</u>	<u>126,607,870</u>
Net assets - End of year	<u>115,826,779</u>	<u>129,701,011</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, 2016

	2016 \$	2015 \$
Cash provided by (used in)		
Operating activities		
Net revenue (expense) for the year	(13,874,232)	3,093,141
Items not affecting cash -		
Realized gain on sale of portfolio investments	(4,784,234)	(8,838,768)
Unrealized (gain) loss on portfolio investments	9,427,929	(9,084,840)
Loss (income) from Queensway Corporate Campus	(265,072)	141,708
Loss (income) from Lisgar Street Property	912	(1,324)
Loss from Michael Street Property	252,577	-
Net change in operating components of working capital -		
Accrued interest receivable	(25,142)	66,186
Accounts receivable	2,956,414	(5,279,088)
Prepaid expenses	(75,090)	25,628
Accounts payable and accrued liabilities	4,874,418	(6,451,046)
Trust liabilities	4,795,955	2,787,491
	<u>3,284,435</u>	<u>(23,540,912)</u>
Investing activities		
Purchase of Lisgar Street Property	-	(1,659,916)
Purchase of Michael Street Property	(4,499,922)	-
Net proceeds (purchases) of project loans receivable	(1,218,103)	945,352
Net proceeds (purchases) of portfolio investments	(4,433,610)	14,324,840
	<u>(10,151,635)</u>	<u>13,610,276</u>
Net change in cash and cash equivalents for the year	(6,867,200)	(9,930,636)
Cash and cash equivalents - Beginning of year	9,155,453	19,086,089
Cash and cash equivalents - End of year	2,288,253	9,155,453

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

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2016

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 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 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, 2016

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 revenues and expenses 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%. As at March 31, 2016, none of this operating credit facility was utilized.

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Notes to Financial Statements

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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, 2016, 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.

Canadian Forces Central Fund

Notes to Financial Statements

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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 Base/Wing/Unit Funds, the Canadian Forces Exchange System (CANEX), Specialty Interest Activities and Messes.

To cover credit losses relating to credit risk and uncollectible accounts, each accounts receivable item purchased from Base/Wing/Unit Funds, CANEX, Specialty Interest Activities and Messes has been assessed a fee to cover an estimated amount that will not be collected. If, at the end of a fiscal year, the actual recovery rate of accounts receivable from a specific entity is different than the fee assessed, the assessed fee is adjusted for the subsequent year. Any amount in excess of the actual credit losses is returned to the entity at the end of each fiscal year.

Accounts receivable are comprised of the following.

	2016 \$	2015 \$
CANEX	60,851,108	55,531,889
CFMWS	949,573	7,605,586
Base/Wing/Funds/Messes	5,612,567	1,458,742
	<u>67,413,248</u>	<u>64,596,217</u>
Trade receivables of CFCF	302,907	6,076,352
	<u>67,716,155</u>	<u>70,672,569</u>
Less: Allowance for doubtful accounts	529,777	529,777
	<u>67,186,378</u>	<u>70,142,792</u>

In regards to the accounts receivable that are assumed on behalf of CANEX, approximately \$57.6 million (2015 - approximately \$53.0 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.

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Accounts payable and accrued liabilities are comprised of the following.

	2016 \$	2015 \$
CANEX	7,462,151	649,477
CFMWS	6,013,759	(296,339)
Base/Wing/Funds/Messes	3,434,837	359,074
	<u>16,910,747</u>	<u>712,212</u>
Trade and other	(3,014,027)	8,310,090
	<u>13,896,720</u>	<u>9,022,302</u>

Included in accounts payable and accrued liabilities at March 31, 2016 are government remittances owing of \$843,484 (2015 - \$1,425,938).

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 2016 or 2015 fiscal years.

	2016 \$	2015 \$
Interest bearing loans	22,253,271	20,782,053
Interest-free loans	4,412,550	4,665,665
	<u>26,665,821</u>	<u>25,447,718</u>
Less: current portion	3,439,424	1,946,414
	<u>23,226,397</u>	<u>23,501,304</u>

Canadian Forces Central Fund

Notes to Financial Statements

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7 Long-term investments

	Market value	2016	Market value	2015
	\$	Cost	\$	Cost
		\$		\$
Portfolio investments				
Canadian stocks	52,487,583	44,401,945	49,519,213	39,260,579
International stocks	49,702,415	35,995,110	52,185,528	33,240,046
Canadian bond fund	60,373,407	60,363,700	61,068,749	59,042,286
	162,563,405	140,760,755	162,773,490	131,542,911

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.

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.

c) The unrealized gain on portfolio investments is calculated as follows.

	2016	2015
	\$	\$
Current year's unrealized gain	21,802,650	31,230,579
Reversal of prior year's unrealized gain	(31,230,579)	(22,145,739)
	(9,427,929)	9,084,840

Canadian Forces Central Fund

Notes to Financial Statements

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8 Equity investments

	2016 \$	2015 \$
Equity in Queensway Corporate Campus	15,098,648	14,833,516
Equity in Lisgar Street Property	1,660,329	1,661,240
Equity in Michael Street Property	4,247,284	-
	<u>21,006,261</u>	<u>16,494,756</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.

	2016 \$	2015 \$
Total assets	48,906,514	50,265,125
Total liabilities	<u>33,807,926</u>	<u>35,431,609</u>
Net assets	<u>15,098,588</u>	<u>14,833,516</u>

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

	2016 \$	2015 \$
Rental revenue	9,560,339	9,236,242
Rental expenses	<u>9,295,267</u>	<u>9,377,950</u>
Net income (loss) for the year	<u>265,072</u>	<u>(141,708)</u>

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

	2016 \$	2015 \$
Cash flows from operating activities	2,591,000	3,076,028
Cash flows from financing activities	(4,171,432)	(2,822,409)
	<u>(1,580,432)</u>	<u>253,619</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.

	2016 \$	2015 \$
Total assets	1,695,824	1,673,032
Total liabilities	35,495	11,792
Net assets	<u>1,660,329</u>	<u>1,661,240</u>

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

	2016 \$	2015 \$
Rental revenue	130,822	62,236
Rental expenses	131,734	60,912
Net income (loss) for the year	<u>(912)</u>	<u>1,324</u>

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

	2016 \$	2015 \$
Cash flows from operating activities	<u>(912)</u>	<u>1,324</u>

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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.

	2016 \$	2015 \$
Total assets	4,264,666	-
Total liabilities	17,382	-
Net assets	<u>4,247,284</u>	<u>-</u>

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

	2016 \$	2015 \$
Rental revenue	-	-
Rental expenses	252,577	-
Net loss for the year	<u>(252,577)</u>	<u>-</u>

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

	2016 \$	2015 \$
Cash flows from operating activities	<u>(252,577)</u>	<u>-</u>

Canadian Forces Central Fund

Notes to Financial Statements

March 31, 2016

9 Trust liabilities

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

	2016 \$	2015 \$
Base funds, messes and others	104,503,789	99,169,595
CANEX	26,155,052	31,919,192
CFMWS	(16,318,107)	(12,720,040)
SOT	15,032,118	8,810,122
Regimental funds and alike	13,749,651	16,188,411
NPF Pension/Benefits	3,273,033	1,220,979
QCC/Lisgar/Michael	3,462,585	470,442
SISIP	588,563	592,028
	<hr/> 150,446,684	<hr/> 145,650,729

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 revenues and expenses of approximately \$303 million and \$301 million for the year ended March 31, 2016, respectively, and net equity of \$740 million at March 31, 2016 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 (2015 - \$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.

Canadian Forces Central Fund

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12 CFCF contributions

During the year, \$564,993 (2015 - \$408,874) was provided by CFCF to programs and distributions provided by CFMWS. CFCF also contributed \$9,295,601 (2015 - \$7,795,508) to Non-Public Fund (NPF) services and operations 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 (2015 - \$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, 2016, this long-term debt of QCC amounted to \$33,291,774 (2015 - \$34,573,255) (note 8).

