Canadian Forces Central Fund

Financial Statements
March 31, 2018

October 10, 2018

Independent Auditor's Report

To the Non-Public Property Board

We have audited the accompanying financial statements of Canadian Forces Central Fund, which comprise the statement of financial position as at March 31, 2018 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.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

PricewaterhouseCoopers LLP
99 Bank Street, Suite 710, Ottawa, Ontario, Canada K1P 1E4
T: +1 613 237 3702, F: +1 613 237 3963

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Canadian Forces Central Fund as at March 31, 2018 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.

Chartered Professional Accountants, Licensed Public Accountants

Canadian Forces Central Fund

Statement of Financial Position

As at March 31, 2018

	2018 $	2017 $
Assets		
Current assets		
Cash (note 4)	15,892,631	-
Accrued interest and dividend receivable	198,659	243,660
Accounts receivable (note 5)	72,628,828	70,689,432
Prepaid expenses	1,618,242	175,132
Current portion of project loans receivable (note 6)	2,421,635	1,887,492
	92,759,995	72,995,716
Other assets		
Project loans receivable (note 6)	37,146,401	38,374,730
Long-term investments (note 7)	167,767,088	177,532,440
Equity investments (note 8)	19,212,351	20,767,619
	316,885,835	309,670,505
Liabilities		
Current liabilities		
Bank overdraft (note 4)	-	3,509,060
Accounts payable and accrued liabilities (note 5)	20,659,055	15,246,533
Trust liabilities (note 9)	165,612,256	152,310,139
	186,271,311	171,065,732
Net Assets	130,614,524	138,604,773
	316,885,835	309,670,505

Approved on Behalf of the Non-Public Property 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, 2018

	2018 $	2017 $
Operating revenue		
Dividends and interest	4,432,914	4,583,587
Realized gain on sale of portfolio investments	9,316,823	11,080,366
Change in unrealized loss on portfolio investments (note 7)	(3,560,090)	(685,138)
Loan interest	1,589,387	944,126
Loss from Queensway Corporate Campus (note 8)	(342,626)	(54,580)
Loss from Lisgar Street Property (note 8)	(75,589)	(228,354)
Gain from Michael Street Property (note 8)	219,332	44,292
Re-insurance guarantee fee (note 10)	250,000	250,000
Other	1,004,272	990,523
	12,834,423	16,924,822
Operating expense		
CFCF management	375,745	276,314
Interest to base/wing funds, messes and trusts	8,048,460	8,306,721
CFMWS user fees for services (note 11)	350,000	350,000
Investment services	281,950	285,598
Other	319,356	895,963
	9,375,511	10,114,596
Net operating revenue before CFCF contributions	3,458,912	6,810,226
CFCF contributions (note 12)		
NPF services and operations	11,556,159	9,032,232
Net expense before other items	(8,097,247)	(2,222,006)
SISIP Financial contribution (note 11)	24,000,000	25,000,000
Writedown of due from CFMWS (note 11)	(23,893,002)	-
Net revenue (expense) for the year	(7,990,249)	22,777,994
Net assets - Beginning of year	138,604,773	115,826,779
Net assets - End of year	130,614,524	138,604,773

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, 2018

	2018 $	2017 $
Cash provided by (used in)		
Operating activities		
Net revenue (expense) for the year	(7,990,249)	22,777,994
Items not affecting cash		
Realized gain on sale of portfolio investments	(9,316,823)	(11,080,366)
Unrealized loss on portfolio investments	3,560,090	685,138
Loss from Queensway Corporate Campus	342,626	54,580
Loss from Lisgar Street Property	75,589	228,354
Disposal of equity investment - Lisgar Street Property	156,385	-
Gain from Michael Street Property	(219,332)	(44,292)
Net change in operating components of working capital		
Accrued interest receivable	45,001	(9,778)
Accounts receivable	(1,939,396)	(3,503,054)
Prepaid expenses	(1,443,110)	51,051
Accounts payable and accrued liabilities	5,412,522	1,349,813
Trust liabilities	13,302,117	1,863,455
	1,985,420	12,372,895
Investing activities		
Disbursements of portfolio	20,000,000	-
Net proceeds (purchases) of project loans receivable	694,186	(13,596,401)
Net purchases of portfolio investments	(4,477,915)	(4,573,807)
Sale of Lisgar Street Property - proceeds	1,200,000	-
	17,416,271	(18,170,208)
Change in cash during the year	19,401,691	(5,797,313)
Cash (bank overdraft) - Beginning of year	(3,509,060)	2,288,253
Cash (bank overdraft) - End of year	15,892,631	(3,509,060)

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

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 Managing Director of NPP 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 (Canada).

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 in the brokers' accounts.

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) 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.

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 the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue 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. The estimates are reviewed annually and as adjustments become necessary, they are recognized in the financial statements in the year 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 its current obligations and management establishes budget and cash estimates to determine its 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%.

Market risk

Market risk is the risk 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 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, 2018, approximately $23.6 million (2017 - $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 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 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/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.

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/Funds/Messes, the Canadian Forces Exchange System (CANEX), specialty interest activities and messes.

Accounts receivable are comprised of the following:

	2018 $	2017 $
CANEX	63,945,036	61,427,060
CFMWS	110,684	128,945
SOT	298,743	610,235
SISIP Financial	4,172	531,002
Base/Wing/Funds/Messes	4,378,119	3,353,529
	68,736,754	66,050,771
Trade and other receivables	4,421,851	5,168,438
	73,158,605	71,219,209
Less: Allowance for doubtful accounts	529,777	529,777
	72,628,828	70,689,432

In regard to the accounts receivable that are assumed on behalf of CANEX, approximately $61.3 million (2017 - approximately $58.7 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 regard to the CANEX credit plans ranging from one-year to three-year plans.

Included in receivables as at March 31, 2018, are net government sales tax remittances owing of $639,363 (2017 - $61,736).

Accounts payable and accrued liabilities are comprised of the following:

	2018 $	2017 $
CANEX	6,812,488	5,710,957
CFMWS	6,068,548	1,797,911
SOT	113,592	123,315
SISIP Financial	87,105	93,955
Base/Wing/Funds/Messes	4,844,890	4,403,174
	17,926,623	12,138,312
Trade and other payables	2,732,432	3,108,222
	20,659,055	15,246,534

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 three 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 2018 or 2017 fiscal years.

	2018 $	2017 $
Interest bearing loans	37,473,986	24,099,447
Interest free loans	2,094,050	16,162,775
	39,568,036	40,262,222
Less: Current portion	2,421,635	1,887,492
	37,146,401	38,374,730

7 Long-term investments

Portfolio investments

	2018		2017	
	Market value $	Cost $	Market value $	Cost $
Cash and cash equivalents	3,413,787	3,413,805	2,170,176	2,204,559
Fixed income	64,035,329	66,818,053	66,461,335	67,971,230
Canadian equities	49,736,445	44,498,780	51,534,924	42,917,975
International equities	50,581,527	35,477,684	57,366,005	43,321,072
	167,767,088	150,208,322	177,532,440	156,414,836

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

Interest rate risk

CFCF 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.

Credit and market risk

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

Withdrawals from the portfolio

$20 million was withdrawn from the portfolio in April 2017 to increase liquity for the support of cash operations.

8 Equity investments

	2018 $	2017 $
Equity in Queensway Corporate Campus	14,701,442	15,044,068
Equity in Lisgar Street Property	-	1,431,974
Equity in Michael Street Property	4,510,909	4,291,577
	19,212,351	20,767,619

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

	2018 $	2017 $
Total assets	46,216,370	48,165,540
Total liabilities	31,514,928	33,121,472
Net assets	14,701,442	15,044,068

- Statement of operations of QCC for the year ended March 31

	2018 $	2017 $
Rental revenue	9,187,058	9,302,836
Rental expenses	9,529,684	9,357,416
Net loss for the year	(342,626)	(54,580)

- Cash flows of QCC for the year ended March 31

	2018 $	2017 $
Cash flows from operating activities	2,743,459	2,008,507
Cash flows from investing activities	(1,960,479)	(2,226)
Cash flows from financing activities	(744,579)	(901,929)
	38,401	1,104,352

Equity in Lisgar Street Property

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

CFCF finalized the sale of the Lisgar Street Property on June 20, 2017 for $1,200,000. The sale price reflected the net book value of the property.

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

	2018 $	2017 $
Total assets	-	1,443,871
Total liabilities	-	11,897
Net assets	-	1,431,974

- Statement of operations of Lisgar Street Property for the year ended March 31

	2018 $	2017 $
Rental revenue	-	42,128
Rental expenses	75,589	270,482
Net loss for the year	(75,589)	(228,354)

- Cash flows of Lisgar Street Property for the year ended March 31

	2018 $	2017 $
Cash flows from operating activities	(1,275,589)	(228,354)
Cash flows from investing activities	1,200,000	-
	(75,589)	(228,364)

Equity in Michael Street Property

The 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

	2018 $	2017 $
Total assets	4,613,917	4,452,759
Total liabilities	103,008	161,182
Net assets	4,510,909	4,291,577

- Statement of operations of Michael Street Property for the year ended March 31

	2018 $	2017 $
Rental revenue	793,141	623,094
Rental expenses	573,809	578,802
Net income for the year	219,332	44,292

- Cash flows of Michael Street Property for the year ended March 31

	2018 $	2017 $
Cash flows from operating activities	219,332	44,292

9 Trust liabilities

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

	2018 $	2017 $
Base funds/messes	101,994,838	98,184,099
CANEX	25,577,353	29,544,434
CFMWS	(2,597,008)	(14,878,418)
SOT	19,219,701	17,511,547
Museums, Regimental Funds and alike (RMC Club)	13,818,223	14,618,568
NPF pension/benefits	4,360,425	3,820,798
QCC/Lisgar/Michael	3,230,494	3,305,879
SISIP Financial	8,230	203,232
	165,612,256	152,310,139

10 Re-insurance guarantee fee

CFCF is contingently liable to a maximum of $100 million as part of the SISIP Financial 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).

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 $440 million and $436 million for the year ended March 31, 2018, respectively, and net equity of $784 million as at March 31, 2018, 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 (2017 - $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 Financial contributed an additional $24,000,000 (2017 - $25,000,000) to CFCF to support NPP programs, capital and operations and maintenance projects. CFCF wrote down the amount due from CFMWS by $23,893,002 related to special pension solvency pension payments and other staff of the NPF employee related costs.

12 CFCF contributions

During the year, $11,556,159 (2017 - $9,032,232) 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 corporate operating costs.

13 Contingent liabilities

CFCF is contingently liable for $44,000 (2017 - $44,000) in letters of credit supplied to various provincial liquor boards on behalf of unit messes.

CFCF, along with CANEX and SISIP Financial, 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. As at March 31, 2018, this long-term debt of QCC amounted to $30,938,348 (2017 - $32,229,809).

14 Comparative figures

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted for the current year.