Giving
Hope
Today

Consolidated **Financial Statements**

The Governing Council of The Salvation Army in Canada

Year Ended March 31, 2017

CONTENTS **PAGE**

Management Commentary

Introduction

These consolidated financial statements present the assets, liabilities, fund balances, revenues, expenses and cash flows of The Governing Council of The Salvation Army in Canada (“The Salvation Army”) and all of the entities it controls for the year ended March 31, 2017. These financial statements were audited by KPMG LLP, Licensed Public Accountants, who issued their opinion on them dated July 10, 2017.

This management commentary has been prepared to assist readers of the financial statements to gain an understanding of The Salvation Army’s financial position and results of operations. It highlights key financial results for the year, as well as key features of The Salvation Army's policy and internal control framework. The framework helps to provide assurance that the financial statements can be relied upon.

Financial Highlights for the Year Ended March 31, 2017

Revenue and Expenses

Overall, revenue increased 27.8% ($180.3 million) in the year ended March 31, 2017. This increase was largely attributable to revenue from investments which moved from a loss of $22.4 million in 2016 to a gain of $126.8 million this year ($149.2 million increase). The rate of return for the year was 13.8% compared to -2.4% in the prior year, driven largely by equities. Excluding the impact of investments, revenue increased 4.6% ($31.2 million) in 2017. The major contributors to this increase were government funding ($9.9 million), Thrift Store sales ($9.8 million) and gain on disposals of tangible capital assets ($8.3 million). Half of the increase in government funding related to funding for a major capital renovation project, while the remainder was funding received for existing or new community programs. Thrift Store sales improved as most store locations experienced increased sales volumes. The sole reason for the increase on the gain on disposal of tangible capital assets was the sale of a significant property in Vancouver. Proceeds from this sale have been reserved for a future building project.

Expenses were 2.0% higher than in the prior year. Although total costs of programs and services increased by only 0.25%, costs for both the territorial and nine divisional headquarters increased by 3.8%, largely as a result of costs that are not expected to recur. Thrift Store expenses increased 5.6% due largely to increased minimum wage levels mandated by provincial legislation and additional costs for three new store openings.

Securities

The management of securities is centralized in the General Investment Fund (“the Fund”), which holds the surplus operating funds, endowments and long-term donor restricted funds for all of the Governing Council's controlled entities. Interest is paid to these controlled entities based on prevailing market rates for similar financial instruments. Net revenue from the Fund is used for the operations of Territorial Headquarters (“THQ”) and Divisional Headquarters (“DHQ”), as well as to make allocations to programs and services.

Allocations from investment revenue are based on a spending policy tied to long term expected rates of return. This approach has the benefit of providing a more stable and predictable level of funding from year to year, mitigating the inherent volatility associated with capital market investment returns. In the year ended March 31, 2017, the Fund gained $126.8 million, incurred expenses of $3.0 million, and paid interest to controlled entities' accounts of $6.1 million, for a net gain of $117.7 million. In accordance with the spending policy, $23.5 million was allocated to operations.

The Fund is managed by external investment managers in accordance with statements of investment policy which establish quality constraints, as well as prohibiting investment in companies whose primary business is the manufacture, distribution or promotion of alcohol, tobacco, pornography, gaming, gaming facilities or armaments and companies that are known to disregard environmental concerns.

The Fund's investment objective is preservation of real (inflation-adjusted) asset value plus a 3.5% to 4.0% annual rate of return, gross of fees, before the impact of withdrawals, over a four-year period. In the four-year period ending March 31, 2017, the Fund earned an average annual return of 9.7%. When the average rate of inflation as measured by the Consumer Price Index of 1.4% is deducted, a real return of 8.3% resulted, well ahead of the investment objective.

Over the ten-year period ended March 31, 2017, the Fund earned an average annual return of 5.8%, or 4.2% in real terms, after deducting average inflation of 1.6%.

Employee Future Benefits

The liability of $156.0 million (2016 - $164.4) for employee future benefits represents the estimated value at March 31, 2017 of the benefits accrued for commissioned officers (see note 9 to the financial statements for additional information on non-commissioned employees).

Benefits for commissioned officers are provided through two plans. The Officers' Retirement Plan is a defined benefit plan registered with the Financial Services Commission of Ontario. This plan provides for basic pension benefits for officers. The supplementary plan provides for additional pension benefits, health care for retirees, and certain lump sum grants.

Actuarial valuations for both plans are performed every three years. The Officers' Retirement Plan, which is funded through a pension trust, was last valued at March 31, 2014. At that time, the Plan had a surplus, measured on a going concern basis (i.e., assuming continued operations), of $22.5 million or 14.5%, and a surplus of $24.9 million or 16.4% on a solvency basis (i.e., assuming the plan were to be wound up on the valuation date). During the year ended March 31, 2017, The Salvation Army made contributions of $3 million to the pension trust.

The supplementary Plan was last valued at March 31, 2015. At that time, the supplementary benefits had an estimated value of $115.4 million, annual service cost to accrue benefits for active officers of $1.8 million and annual benefit payments to retired officers of $6.1 million. No assets are set aside to fund the benefit payments; they are paid from general revenues when incurred.

The financial statements reflect actuarial estimates as at March 31, 2017. The next actuarial valuations for both plans will be conducted as at March 31, 2017, but the results are not yet available.

Long-Term Debt

The Salvation Army avoids debt financing, except for the acquisition and/or development of land and buildings. Total loans and mortgages payable ($68.8 million long-term and $17.8 million short-term) declined by $4.7 million from the prior year as a result of principal repayments of $8.6 million and new financing arrangements put in place during the year of $3.9 million. The fact that several of these obligations are up for renewal in the next year explains the increase in short-term loans and mortgages payable and the offsetting decrease in the long-term portion.

Financial Position

As at March 31, 2017, The Salvation Army's total assets were $1.81 billion, compared to $1.69 billion at the prior year end. This increase was largely attributable to the increase in the value of securities. Additions to capital assets and an increase in cash and cash equivalents are other contributing factors.

The Salvation Army's net assets, or fund balances, totalled $1.48 billion, up $141.1 million from the prior year. Of the total:

- $586.4 million represents funds invested in capital assets, predominantly land and buildings;
- $32.4 million represents funds held in endowments that are externally restricted in perpetuity; and
- $31.0 million represents funds held in endowments established internally to provide income for specified programs on an ongoing basis.

The remaining $827.1 million (2016 - $702.4) represents the net funds being held for allocation to future operations, as follows:

	2017	2016
Externally restricted funds	$177.3	$181.0
Internally restricted funds		
Investment earnings spending policy reserve	$363.4	$269.7
Other internally restricted funds	$256.7	$252.6
Unrestricted funds		
Operating funds	$103.7	$103.6
Re-measurement of employee future benefits	($74.0)	($104.5)
	$827.1	**$702.4**

The Salvation Army's target is to have sufficient unrestricted operating funds to meet at least three months' operating expenses. Only 66% of ministry units met this target at March 31, 2017, compared to 58% in the prior year. On an overall basis, the total operating funds of $103.7 million represent sufficient funds to meet approximately 1.9 months' operating expenses, which is consistent with the prior year.

A plan is in place to fund the re-measurement deficiency over the remaining service life of the employees for whom benefits are provided, which was estimated at 12.3 years as of March 31, 2017, compared with 10.9 years at March 31, 2016.

The Salvation Army takes its stewardship responsibility seriously. The desire to release funds for its work as quickly and as effectively possible must be balanced with the need to ensure its long-term financial viability so as to be able to maintain programs and services in the future. We believe that we are managing this tension well.

Governance

Information concerning The Salvation Army's overall governance structure can be found in the Annual Review report (**www.salvationarmy.ca/annualreview**). The following committees play key roles with respect to financial management and internal control over financial reporting.

Territorial Finance Council

The Territorial Finance Council, a committee of the Territorial Management Board, is charged with the oversight of the management of all financial and property resources of The Salvation Army in Canada and Bermuda.

Member	Office held (if any)	Date Appointed	Number of meetings eligible to attend in 2016/17	Number of meetings attended in 2016/17
Commissioner Susan McMillan, *BAS, MBA, CPA, CGA* Territorial Commander	Chair	September 1, 2014	20	19
Colonel Mark Tillsley, *MSW, Ph.D.* Chief Secretary	Vice-Chair	June 1, 2013 to December 31, 2016	15	12
Colonel Lee Graves, *MBA* Chief Secretary	Vice-Chair	July 1, 2013 Vice-Chair, Jan 1, 2017	20	18
Mr. R. Paul Goodyear, *B.Com, MBA, FCPA, FCMA* Financial Secretary	Secretary	July 1, 2001	20	15
Lt.-Colonel Marsha-Jean Bowles Secretary for Program		January 1, 2017	5	3
Lt.-Colonel Jamie Braund, *B.Sc., MAL* Secretary for Personnel		July 1, 2014	20	19
Lt.-Colonel James Champ, *BRE, MBA* Secretary for Communications		July 1, 2013	20	15
Mr. David Dunstan, *B.Com., CPA, CMA* Assistant Financial Secretary		August 1, 2012	20	16
Ms. Mary Ellen Eberlin, *BScN, MScN* Territorial Social Services Secretary		September 1, 2013	20	17
Dr. Marjory Kerr President, Booth University College		January 1, 2017	5	4
Mr. Graham Moore, *B.Com., MBA, CPA, CMA* Director of Organizational Development		September 1, 2013	20	19
Major Shona Pike, *BA* Secretary for Candidates		September 1, 2015	20	15
Lt.-Colonel Fred Waters, *MA* Secretary for Business Administration		September 1, 2013	20	17

Audit Committee

During the year, The Salvation Army established an Audit Committee, which is responsible for overseeing financial reporting, including the quality and integrity of The Salvation Army's financial statements and disclosures, internal control over the financial reporting process, and legal and regulatory requirements.

The Committee reviews the audited consolidated financial statements and assesses:

- the quality and appropriateness of the principles and policies used in preparing the statements, including any changes in accounting principles and/or policies that are proposed;
- significant estimates used in preparing the financial statements; and
- significant variances from plans or comparable results of prior periods.

The Committee discusses the financial statements and auditors' report with the external auditors and management, and recommends the approval of the statements to the Governing Council.

The Committee is responsible for oversight of The Salvation Army's relationship with the external auditor, and recommends the appointment or replacement of the auditor to the Governing Council as well as the proposed compensation for the services to be provided.

The Committee is responsible for oversight of management's establishment of an adequate system of internal control, considers the integrity of the financial reporting process, and discusses significant financial risk exposures.

The Committee has been established with three external members, who are not employed by The Salvation Army, and two members of the Governing Council. Although management of the finance and internal audit functions attend meetings to provide staff support, the Committee also meets independently with the external auditors, without members of the Governing Council or management present.

Member	Office held (if any)	Date Appointed	Number of meetings eligible to attend in 2016/17	Number of meetings attended in 2016/17
Patricia L. O'Malley, *B.Comm., FCPA, FCA* Board Director and Independent Financial Reporting Consultant *	Chair	January 1, 2017	2	2
Mr. Brian W. Barrington, *CPA, CA* Independent Accounting Professional *		January 1, 2017	2	2
Ms. Annie Giraudou, *CPA, CA, MBA, FLMI, CFSA, CRMA, ASC* Senior Vice-President and Chief Risk Officer, Ivanhoé Cambridge *		January 1, 2017	2	2
Colonel Lee Graves, *MBA* Chief Secretary		January 1, 2017	2	2
Lt.-Colonel Fred Waters, *MA* Secretary for Business Administration		January 1, 2017	2	2

* denotes volunteer members

Investment Advisory Committee

The Investment Advisory Committee is responsible for making recommendations to the Territorial Finance Council with respect to The Salvation Army's investment policies and structures. The Committee reviews the statements of investment policy and makes recommendation for revisions, as appropriate; oversees the recruitment and selection of investment management firms, and makes recommendations for their engagement; monitors the performance of The Salvation Army's portfolios and ensures they are managed to achieve optimal long-term performance to meet The Salvation Army's needs, in accordance with the statements of investment policy.

Member	Office held (if any)	Date Appointed	Number of meetings eligible to attend in 2016/17	Number of meetings attended in 2016/17
Mr. William Chinery, *B.Math., FCIA, FSA, CFA* Independent Investment Professional *	Chair	January 1, 2011	4	4
Mr. William J. Stafford, *B.Comm., MBA, CFA* Director of Investments	Secretary	October 1, 2001	4	4
Mr. David Dunstan, *B.Com., CPA, CMA* Assistant Financial Secretary		January 1, 2017	2	2
Mr. Kevin Fahey, *B.Comm., LL.B., CFA* Director, Investments Colleges of Applied Arts & Technology Pension Plan *		September 1, 2010	4	3
Mr. Michael Gallimore, *B.Comm., MBA, CFA* Independent Investment Professional *		June 5, 2013	4	4
Mr. R. Paul Goodyear, *B. Comm., MBA, FCPA, FCMA* Financial Secretary		October 1, 1998	4	4
Lt.-Colonel Lee Graves, *MBA* Secretary for Business Administration		July 1, 2014 to December 31, 2016	2	2
Mr. Yannick Ménard, *B.Sc., CFA, FCIA, FSA* Managing Director, Pension Investments BMO Bank of Montreal *		July 29, 2013	4	4
Lt.-Colonel Fred Waters, *MA* Secretary for Business Administration		January 1, 2017	2	1
Ms. Mary Ann Wiley, *BA, CFA* Independent Investment Professional *		January 1, 2017	2	2

* denotes volunteer members

Internal Controls

The Salvation Army has a strong internal control environment to protect The Salvation Army's assets and facilitate accuracy in financial reporting.

The Audit Committee has overall responsibility for internal controls over financial reporting. The Internal Audit Advisory Committee provides oversight of the internal audit function. The Internal Audit Department performs audits and other work to determine the extent to which internal controls are operating effectively and how any deficiencies should be remediated.

In addition to Canadian external and internal audits, The Salvation Army is also subject to triennial audits by an audit team from its International Headquarters (IHQ) in London, England. The most recent audit conducted in 2014, covering the period from April 1, 2011 to March 31, 2014, concluded that The Salvation Army in Canada and Bermuda "is in a sound financial position which can be largely attributed to careful management and the prudent use of volatile income streams…" The findings and recommendations include no high risk issues, one medium risk issue (the rebuilding of the operating fund balance, which was depleted with the recognition of all pension and post-retirement obligations) and three low risk issues. A long-term plan is in place to address the medium risk issue, as noted earlier in this report, and the low risk issues have all been addressed. The next audit is scheduled to take place in the fall of 2017.

Both a code of conduct (**www.salvationarmy.ca/Code-of-Conduct**) and a whistleblower policy (**www.salvationarmy.ca/whistleblower-policy**) are in place. The former sets out expectations for behaviour by all staff and volunteers, while the latter provides a mechanism for making anonymous complaints when violations of the code and other key policies are observed. During the year ended March 2017, no complaints were received with respect to alleged breaches by individuals who had an oversight role in financial reporting.

Staff Compensation

The Salvation Army employs both commissioned officers and lay staff. The compensation package for all commissioned officers of The Salvation Army includes housing, with furnishings and utilities provided by The Salvation Army, a leased vehicle or vehicle allowance, and a cash allowance based on years of service. The cost of allowances and benefits provided to senior officers is believed to be significantly lower than that paid to executives in other similar organizations for positions of comparable responsibility. The total employment income for income tax purposes reported in 2016 for the five most senior commissioned officers of The Salvation Army in Canada (including cash, as well as housing, automobile and other benefits), ranged from $41,256 to $69,531, with an average of $48,173.

The size and scope of The Salvation Army's operations create a level of complexity that requires the hiring of highly skilled professional and technical staff to supplement the skills found in its commissioned officer ranks. These salaries are typically less than comparable positions in the for-profit sector. However, significant competition exists for professional staff in the not-for-profit sector. As a result, compensation in the not-for-profit sector has increased in recent years in order to attract and retain requisite expertise.

In the 2016 calendar year, there were 89 non-commissioned employees whose total employment income (including salaries and benefits) reported for income tax purposes was above $100,000, as follows:

Compensation range	Number of employees
$100,000 - $119,999	60
$120,000 - $149,999	13
$150,000 - $199,999	13
$200,000 - $249,999	2
$250,000 - $299,999	0
$300,000 - $349,999	1

Paying competitive salaries to attract the right people on the one hand, and ensuring that compensation levels are as efficient and as appropriate on the other creates tension. This tension is particularly acute in the not-for-profit sector where organizations and donors are both concerned about keeping administrative costs at a reasonable level so as to maximize funds available for direct service delivery. The Salvation Army strives to employ highly qualified people, while at the same time managing its resources in a prudent manner.

Fundraising

For 135 years, faithful donors have helped The Salvation Army carry on its tradition of caring for vulnerable men, women and children in Canada, Bermuda and around the world. The Salvation Army is deeply grateful for their generosity and for the trust they have shown in us to use their investment wisely.

During the fiscal year ended March 31, 2017, supporters made donations to The Salvation Army totaling $187.5 million, compared to $189.7 million the previous year, a decrease of 1.2%. Fundraising costs are the total costs incurred by the public relations and development department. For the same period these costs were $22.7 million, compared to $22.9 million last year. As a proportion of charitable donations, these costs represented 12.1%, identical to the prior year, with an average of 11.9% per year for the past five years. The Salvation Army does not allocate any costs incurred by the Public Relations and Development Department to functions other than fundraising. Arguably, this means that the actual average fundraising costs are below 11.9% because much of the public relations work is educational rather than soliciting for donations. This compares very favourably to the Canada Revenue Agency upper limit of 35%.

At the same time, it should be recognized that the "fundraising costs as a proportion of charitable donations" measure has several limitations as an indicator of effectiveness. First, no donations of materials (e.g., to Thrift Stores) or services are recognized in these financial statements, even though costs are incurred in obtaining these donations. Second, as the name implies, some of the activity these costs represent relates to general marketing and communication functions, rather than fundraising activities. Third, the costs of the Planned Giving program and expenses related to the generation of planned gifts, particularly legacies and estates, are generally not incurred in the same year in which the revenues occur. Fourthly, fundraising effectiveness may not be optimized by low fundraising costs as a greater fundraising investment may yield additional donations. The Salvation Army reviews its fundraising efforts on an ongoing basis with an objective to find the right balance between effectiveness and efficiency of its fundraising activities.

Costs of Administration

Many stakeholders are interested in how much a charity spends on its administration and management versus programs and services. The Salvation Army currently classifies all activities and functions at the operating unit level as programs and services. Only activities at the territorial and divisional headquarters level are attributed to administration. Over the five-year period ended March 2017, territorial and divisional headquarters operating costs, other than those expenses related directly to program and services provision or support, such as the development of program resources, etc., represented, on average, 5.3% of total expenses.

While this is low by comparison to many other charities, The Salvation Army cautions stakeholders with respect to the conclusions they may draw based on this single indicator. While it is generally true that it is an indicator of overall efficiency, it does not necessarily measure effectiveness of program outcomes.

In addition, this indicator does not provide a reasonable comparator across organizations. Typically, smaller organizations lack the economies of scale that help larger organizations achieve lower ratios, while fundraising organizations will tend to have lower ratios than charities delivering services.

Administration and management functions are as essential to effective outcomes as direct programs and services. Without them, charities such as The Salvation Army would be much less successful. As a result, undue focus on minimizing administration and management costs can have a negative impact on operations.

The Salvation Army is committed to ensuring that its administrative costs remain appropriate for the size and complexity of the organization and to effectively supporting its varied programs and service delivery.

Privacy

The Salvation Army is committed to protecting the privacy of its donors, customers, clients, volunteers, employees, and members, and is always concerned with treating personal information carefully and with appropriate confidentiality. Personal information is not used or disclosed for purposes other than those for which it was collected, except with consent or as required by law. This information is retained only as long as necessary and The Salvation Army does not trade, rent or sell any personal information to third parties.

Donations

The Salvation Army will accept unrestricted gifts, as well as gifts restricted for specific programs and purposes, provided that such gifts are consistent with its stated mission, purposes, and priorities. Gifts may be restricted to specific Salvation Army programs/purposes or communities throughout Canada and around the world where The Salvation Army has established operations.

After a gift has been accepted, if circumstances should at any time make it impractical, in the view of The Salvation Army acting reasonably, to apply the gift to the designated purpose, it may re-designate the purpose of the gift using its best efforts to adhere as closely as possible to the original intent of the gift.

Except as directed otherwise by the donor, The Salvation Army uses funds raised in public appeals for its community and social services programs and activities, rather than for its corps and congregational ministries.

Imagine Canada Standards Program

The Salvation Army places accountability at the core of its relationships with its donors and members of the public. In 2015, The Salvation Army was accredited by Imagine Canada's Standards Programs for charities and nonprofit organizations. The accreditation recognizes excellence in accountability, transparency and governance.

STRONG CHARITIES. STRONG COMMUNITIES. ACCREDITED SINCE 2015 IMAGINE CANADA

Management Responsibility for Financial Reporting

These consolidated financial statements are the responsibility of management. They have been prepared in accordance with Canadian generally accepted accounting principles for not-for-profit organizations, as established by the Canadian Accounting Standards Board.

The preparation of financial information is an integral part of the ongoing management of The Salvation Army. Management has established internal control systems to ensure that all financial details are objective and reliable, and that the organization's assets are safeguarded.

The Governing Council has overall responsibility for the financial statements, assisted by the Audit Committee, which meets regularly with management as well as internal and external auditors to ensure the adequacy of internal controls over financial reporting, and to review the financial statements and external auditors' report. The Governing Council appoints the external auditors and approves the financial statements, based on recommendations from the Audit Committee.

The financial statements have been audited by external auditors KPMG LLP, Chartered Professional Accountants and Licensed Public Accountants. Their report outlines the scope of KPMG's examination and presents their opinion on the financial statements.

Lieut.-Colonel Fred Waters, MA
Territorial Secretary for Business Administration
and Treasurer of The Governing Council

Mr. R. Paul Goodyear, MBA, FCPA, FCMA
Territorial Financial Secretary
and Secretary of The Governing Council

July 10, 2017

KPMG

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INDEPENDENT AUDITORS' REPORT

To The Governing Council of
The Salvation Army in Canada

We have audited the accompanying consolidated financial statements of The Governing Council of The Salvation Army in Canada, which comprise the consolidated balance sheet as at March 31, 2017, the consolidated statements of operations, changes in fund balances and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated 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 consolidated financial statements.

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

Basis for Qualified Opinion

In common with many charitable organizations, The Governing Council of The Salvation Army in Canada derives revenue from charitable donations, the completeness of which is not susceptible to satisfactory audit verification. Accordingly, verification of this revenue was limited to the amounts recorded in the records of The Governing Council of The Salvation Army in Canada. Therefore, we were not able to determine whether, as at and for the years ended March 31, 2017 and March 31, 2016, any adjustments might be necessary to charitable donations and excess (deficiency) of revenue over expenses reported in the consolidated statements of operations, excess (deficiency) of revenue over expenses reported in the consolidated statements of changes in fund balances and excess (deficiency) of revenue over expenses reported in the consolidated statements of cash flows and assets and fund balances reported in the consolidated balance sheets. This caused us to qualify our opinion on the consolidated financial statements as at and for the year ended March 31, 2016.

Qualified Opinion

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of The Governing Council of The Salvation Army in Canada as at March 31, 2017, and its consolidated results of operations and its consolidated cash flows for the year then ended in accordance with Canadian accounting standards for not-for-profit organizations.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

July 10, 2017
Vaughan, Canada

THE GOVERNING COUNCIL OF THE SALVATION ARMY IN CANADA

Consolidated Balance Sheet
(In thousands of dollars)

March 31, 2017, with comparative information for 2016

	2017	2016
Assets		
Current assets:		
Cash and cash equivalents	$ 53,387	$ 31,549
Receivables and other current assets	27,766	32,437
	81,153	63,986
Securities (note 4)	1,019,302	939,008
Tangible capital assets (note 6)	707,006	684,564
Other assets (note 7(a))	4,801	4,601
	$ 1,812,262	$ 1,692,159
Liabilities and Fund Balances		
Current liabilities:		
Accounts payable and accrued liabilities	$ 53,846	$ 59,032
Deferred revenue	17,490	17,538
Current portion of loans and mortgages payable (note 8)	17,766	10,088
	89,102	86,658
Long-term liabilities:		
Employee future benefits (note 9(a))	155,986	164,367
Loans and mortgages payable (note 8)	68,838	81,171
Deposits on life leases (note 10)	11,805	12,155
Other liabilities (notes 7(b) and 9(b))	9,585	11,985
	246,214	269,678
Fund balances:		
Operating (note 11(a))	29,715	(873)
Endowment (note 11(b))	63,449	62,976
Other Restricted (note 11(c))	797,429	703,281
Capital	586,353	570,439
	1,476,946	1,335,823
Contingencies and commitments (notes 16 and 17)		
	$ 1,812,262	$ 1,692,159

See accompanying notes to consolidated financial statements.

On behalf of The Governing Council:

_________________________ Secretary

_________________________ Treasurer

THE GOVERNING COUNCIL OF THE SALVATION ARMY IN CANADA

Consolidated Statement of Operations
(In thousands of dollars)

Year ended March 31, 2017, with comparative information for 2016

	2017					2016				
	Operating Fund	Restricted Funds Endowment	Restricted Funds Other	Restricted Funds Capital	**Total**	Operating Fund	Restricted Funds Endowment	Restricted Funds Other	Restricted Funds Capital	**Total**
Revenue:										
Charitable donations	$ 108,653	$ 293	$ 78,435	$ 83	**$ 187,464**	$ 108,845	$ 499	$ 80,223	$ 88	**$ 189,655**
Government funding	225,189	–	514	12,670	**238,373**	219,775	–	948	7,707	**228,430**
Fees for service	80,758	–	–	–	**80,758**	78,713	–	–	–	**78,713**
Investment income (loss) (note 12)	125,899	–	876	–	**126,775**	(23,569)	–	1,181	–	**(22,388)**
Thrift stores	153,310	–	–		**153,310**	143,506	–	–	–	**143,506**
Gain on disposal of tangible capital assets	–	–	–	24,293	**24,293**	–	–	–	15,972	**15,972**
Other	17,490	–	597	1,060	**19,147**	15,471	–	155	284	**15,910**
	711,299	293	80,422	38,106	**830,120**	542,741	499	82,507	24,051	**649,798**
Expenses (note 13):										
Charitable programs and services:										
Addictions, corrections and residential	178,061	–	–	–	**178,061**	174,939	–	–	–	**174,939**
Health care	124,965	–	–	–	**124,965**	123,866	–	–	–	**123,866**
Community and family services	63,126	–	–	–	**63,126**	61,712	–	–	–	**61,712**
Congregational ministries	48,873	–	–	–	**48,873**	51,961	–	–	–	**51,961**
Children and youth	15,572	–	–	–	**15,572**	15,453	–	–	–	**15,453**
Educational	8,038	–	–	–	**8,038**	7,712	–	–	–	**7,712**
Overseas development – and missions	541	–	4,198	–	**4,739**	502	–	6,228	–	**6,730**
Other programs and services	11,487	–	–	–	**11,487**	11,373	–	–	–	**11,373**
	450,663	–	4,198	–	**454,861**	447,518	–	6,228	–	**453,746**
Thrift stores	138,422	–	–	–	**138,422**	131,032	–	–	–	**131,032**
Headquarters' operating	37,649	–	–	–	**37,649**	36,271	–	–	–	**36,271**
Public relations and development	11,405	–	11,265	–	**22,670**	12,329	–	10,569	–	**22,898**
Amortization	–	–	–	30,482	**30,482**	–	–	–	30,206	**30,206**
Other	14,667	–	–	2,325	**16,992**	13,381	–	–	120	**13,501**
	652,806	–	15,463	32,807	**701,076**	640,531	–	16,797	30,326	**687,654**
Excess (deficiency) of revenue over expenses	$ 58,493	$ 293	$ 64,959	$ 5,299	**$ 129,044**	$ (97,790)	$ 499	$ 65,710	$ (6,275)	**$ (37,856)**

See accompanying notes to consolidated financial statements.

THE GOVERNING COUNCIL OF THE SALVATION ARMY IN CANADA

Consolidated Statement of Changes in Fund Balances
(In thousands of dollars)

Year ended March 31, 2017, with comparative information for 2016

2017	Operating Fund (note 11(a))	Restricted Funds: Endowment (note 11(b))	Restricted Funds: Other (note 11(c))	Restricted Funds: Capital	Total
Fund balances, beginning of year	$ (873)	$ 62,976	$ 703,281	$ 570,439	$ 1,335,823
Excess of revenue over expenses	58,493	293	64,959	5,299	129,044
Change in cumulative translation adjustment	350	–	–	–	350
Remeasurement and other items (note 9(a))	11,729	–	–	–	11,729
Net interfund transfers (note 14)	(39,984)	180	29,189	10,615	–
Fund balances, end of year	$ 29,715	$ 63,449	$ 797,429	$ 586,353	$ 1,476,946

2016	Operating Fund (note 11(a))	Restricted Funds: Endowment (note 11(b))	Restricted Funds: Other (note 11(c))	Restricted Funds: Capital	Total
Fund balances, beginning of year	$ (5,075)	$ 66,055	$ 708,863	$ 594,554	$ 1,364,397
Excess (deficiency) of revenue over expenses	(97,790)	499	65,710	(6,275)	(37,856)
Change in cumulative translation adjustment	781	–	–	–	781
Remeasurement and other items (note 9(a))	8,501	–	–	–	8,501
Net interfund transfers (note 14)	92,710	(3,578)	(71,292)	(17,840)	–
Fund balances, end of year	$ (873)	$ 62,976	$ 703,281	$ 570,439	$ 1,335,823

See accompanying notes to consolidated financial statements.

THE GOVERNING COUNCIL OF THE SALVATION ARMY IN CANADA

Consolidated Statement of Cash Flows
(In thousands of dollars)

Year ended March 31, 2017, with comparative information for 2016

	2017	2016
Cash provided by (used in):		
Operating activities:		
Excess (deficiency) of revenue over expenses	$ 129,044	$ (37,856)
Items not affecting cash (note 15(a))	(81,387)	75,507
Change in non-cash operating working capital (note 15(b))	(563)	1,029
Contributions to other retirement benefits	(4,552)	(4,024)
Contributions to defined benefit and supplementary retirement pension plans	(4,715)	(4,667)
	37,827	29,989
Financing activities:		
Decrease (increase) in other assets	(200)	734
Repayment of loans and mortgages	(8,689)	(8,895)
Increase in loans and mortgages	4,034	2,986
Decrease in other liabilities	(2,415)	(798)
Decrease in deposits on life leases	(350)	(82)
	(7,620)	(6,055)
Investing activities:		
Sale (purchase) of securities, net	19,912	(14,022)
Additions to tangible capital assets	(59,564)	(44,989)
Proceeds on disposal of tangible capital assets	30,933	22,460
	(8,719)	(36,551)
Change in cumulative translation adjustment (note 11(a))	350	781
Increase (decrease) in cash and cash equivalents	21,838	(11,836)
Cash and cash equivalents, beginning of year	31,549	43,385
Cash and cash equivalents, end of year	$ 53,387	$ 31,549

See accompanying notes to consolidated financial statements.

The Governing Council of The Salvation Army in Canada ("The Governing Council"), a corporation established by a Special Act of Parliament, is the primary legal entity through which The Salvation Army, an international movement, conducts its operations in Canada. The Governing Council is a religious, charitable and not-for-profit organization, registered by Canada Revenue Agency for tax-deductible contributions, with the territorial headquarters ("THQ") in Toronto as the main charity, and every other Salvation Army operation registered as an associated charity of THQ. The Salvation Army Corporation of Bermuda is a controlled entity through which The Governing Council conducts its operations in Bermuda.

The Salvation Army is an evangelical part of the universal Christian Church. Its message is based on the Bible. Its ministry is motivated by love for God. Its mission is to share the love of Jesus Christ, meet human needs and be a transforming influence in the communities of the world.

The Salvation Army in Canada and Bermuda (the "Army") comprises over 400 controlled entities ("ministry units"), with operations including corps (churches), community centres, long-term care facilities, hospices and a hospital, transitional housing and shelters, addictions and rehabilitation centres, thrift stores and other social programs.

1. Basis of presentation:

These consolidated financial statements present, in accordance with Canadian accounting standards for not-for-profit organizations in Part III of the Chartered Professional Accountants of Canada ("CPA Canada") Handbook, the assets, liabilities, fund balances, revenue, expenses and cash flows of The Governing Council and its controlled entities.

(a) Operating Fund:

The purpose of the Operating Fund is to record the administrative and operating activities of the Army. This includes the operations of THQ and the nine divisional headquarters ("DHQ"), the College for Officer Training, William & Catherine Booth University College, National Recycling Operations ("NRO"), Grace Communities Corporation ("GCC") and all programs operated at ministry units.

1. Basis of presentation (continued):

(b) Restricted Funds:

(i) Endowment Fund:

The purpose of the Endowment Fund is to record the accumulation of externally restricted endowment contributions and unrestricted amounts internally designated as endowments.

External restrictions refer to any conditions or specific uses that have been requested or required by the donors in making a gift to the Army. Internal restrictions refer to those funds which management has earmarked for specific purposes, which are not subject to any donor or other restrictions on their use.

(ii) Other Restricted Funds:

The Other Restricted Funds record receipt and use of funds that are both externally and internally restricted (note 11(c)), other than Endowment Fund or Capital Fund items.

Externally restricted funds include receipt of funds for the National Red Appeal campaigns (used to support the social and community services work of the Army in Canada and Bermuda), donations and legacies with external restrictions, other than endowments, as well as the receipt and use of funds for the World Services Appeal campaigns (used to support the work of the Army internationally).

Internally restricted funds represent reserves designated by the Army for specific purposes, including future years' operations. Included in internally restricted funds is the Army's excess investment earnings reserve. Under Army policy, investment earnings are allocated for operations based on an expected long-term rate of return. In years when actual earnings are greater, the excess is placed in reserve for future years when actual earnings are less than the expected long-term rate of return. This approach helps mitigate the impact of inherent volatility in the capital markets on the Army's operations.

1. Basis of presentation (continued):

(iii) Capital Fund:

The purpose of the Capital Fund is to record all transactions related to the acquisition and improvement of tangible capital assets, as well as the related debt and net investment of the Army in such assets.

2. Significant accounting policies:

(a) Cash and cash equivalents:

The Army considers deposits in banks, certificates of deposit and other short-term investments with original maturities of 90 days or less at the date of acquisition and held for operating purposes as cash and cash equivalents. From time to time, the long-term investment portfolio, while having no policy allocation to cash and cash equivalents, holds cash and cash equivalents as a short-term tactical strategy. Such investments are shown as securities in the non-current assets section of the consolidated balance sheet as they are not used for current operating needs.

(b) Financial instruments:

Financial instruments are recorded at fair value on initial recognition. The Army has elected to carry all securities at fair value and as a result, they are revalued monthly. All other financial instruments are subsequently recorded at cost or amortized cost.

Transaction costs incurred on the acquisition of securities are expensed as incurred. All other financial instruments are adjusted by transaction costs incurred on acquisition and financing costs, which are amortized using the straight-line method.

Receivables are assessed for impairment on an annual basis at the end of the fiscal year. If there is an indicator of impairment, the Army determines if there is a significant adverse change in the expected amount or timing of future cash flows from the financial asset. If there is a significant adverse change in the expected cash flows, the carrying value of the financial asset is reduced to the highest of the present value of the expected cash flows, the amount that could be realized from selling the financial asset or the amount the Army expects to realize by exercising its right to any collateral. If events and circumstances reverse in a future year, an impairment loss is reversed to the extent of the improvement, not exceeding the initial carrying value.

2. Significant accounting policies (continued):

(c) Interest rate hedging:

The Army uses interest rate swaps to manage fluctuations in interest rates on some long-term mortgages. The Army uses the accrual basis of accounting for hedges. Gains or losses realized on the settlement of the hedging item are deferred until the settlement of the hedged item.

At the inception of the hedging relationship, the Army designates that hedge accounting will be applied. The Army formally documents the hedging relationship between the hedging instruments and hedged items. At the inception of the hedge and throughout its term, the terms of the hedging item and hedged item are the same.

Hedge accounting is used only when the notional amount of the swap matches the principal amount of the hedged item, the fair value of the swap at the inception is nil, the fixed rate is the same throughout the swap, the variable rate is based on the same index and includes the same or no adjustment, the debt instrument cannot be settled before maturity, and the swap matures within two weeks of the maturity date of the debt.

(d) Tangible capital assets:

Land is carried at cost if purchased or at fair value if donated, at the date of acquisition and is not amortized.

Land improvements, buildings and vehicles are stated at cost, less accumulated amortization. Amortization is provided on a straight-line basis over their estimated useful lives of 15 years, 40 years and 5 years, respectively.

Furniture and equipment with original cost exceeding $5 is stated at cost, less accumulated amortization. Amortization is computed on a straight-line basis over their estimated useful lives ranging from 3 to 10 years.

(e) Contributions of materials and services:

The Army receives contributions of goods and materials, as well as volunteer time and services in the delivery of its programs. The value of these contributions is not recognized in these consolidated financial statements.

2. Significant accounting policies (continued):

(f) Revenue recognition:

The Army follows the restricted fund method of accounting for restricted contributions and endowments. Restricted contributions and endowments are recognized as revenue of the appropriate restricted fund. When a restricted contribution is received for which there is not a restricted fund established, the contribution is deferred in the Operating Fund and recognized as revenue in the year in which the related expenses are incurred.

Charitable donations include legacies which are recorded when received.

Government funding and fees for service are recognized as revenue when received or receivable if the amount to be received can be reasonably estimated and collection is reasonably assured.

Investment income includes interest income, dividends, net realized gains on the sale of securities and change in net unrealized gain (loss) on securities. Interest income earned on restricted funds is recognized in the Other Restricted Funds, while other investment income is recorded in the Operating Fund.

Thrift stores revenue includes sales of used clothing and other goods that have been donated to NRO and ministry unit operated thrift stores. Revenue is recognized at the point of sale.

(g) Employee future benefits:

(i) Officers' retirement benefits:

The Army maintains a non-contributory defined benefit pension plan for all commissioned officers and auxiliary-captains. Commissioned officers are enrolled in the plan at the date of commissioning and auxiliary-captains at the date of warranting. Individuals who successfully complete the required period of training, are commissioned as officers and ordained as ministers of the Gospel of Jesus Christ. Officers of the Army have relinquished secular employment in response to a spiritual calling, so as to devote all their time and energies to the service of God and the people. The Army also provides other retirement benefits to eligible officers. Other retirement benefits include supplementary allowances and medical and dental benefits. The Army uses actuarial reports prepared by independent actuaries as the basis for its funding decisions.

2. Significant accounting policies (continued):

The Army accrues its obligations under benefit plans and the related costs, net of plan assets. The following policies have been adopted:

(a) the cost of pensions and the other retirement benefits earned by officers are actuarially determined using the projected benefit method prorated on service and management's best estimate of expected plan investment performance, salary escalation, retirement ages of officers and expected health care costs;

(b) the plan assets, which are recorded at fair value, and the accrued benefit obligation are measured at March 31 of each year;

(c) the discount rate used to determine the accrued benefit obligation is determined by reference to market interest rates at the measurement date on high-quality debt instruments with cash flows that match the timing and amount of expected benefit payments;

(d) actuarial gains (losses) on plan assets arising from the difference between the actual and expected return on plan assets for a period are immediately recognized in the consolidated statement of changes in fund balances. For the purpose of calculating the expected return on plan assets, the assets are valued at fair value. Actuarial gains (losses) on the accrued benefit obligation that arise from differences between actual and expected experience and from the changes in the actuarial assumptions used to determine the accrued benefit obligation are immediately recognized in the consolidated statement of changes in fund balances; and

(e) past service costs arising from plan amendments are recognized immediately in the consolidated statement of changes in fund balances.

(ii) Employees' retirement benefits:

The Army makes regular contributions to a group Registered Retirement Savings Plan, administered by a third party, on behalf of each eligible employee. All permanent full-time and part-time employees are eligible for enrolment in the plan following completion of three months of continuous service.

2. Significant accounting policies (continued):

(h) Translation of foreign currencies:

Assets and liabilities denominated in foreign currencies have been translated into Canadian dollars at exchange rates prevailing at the year-end date. Revenue and expenses and allocations have been translated using exchange rates prevailing on the transaction date.

Exchange gains and losses arising from the translation of the consolidated financial statements of The Salvation Army Corporation of Bermuda, a self-sustaining foreign operation are recognized in the Operating Fund balances on the consolidated balance sheet.

(i) GCC life leases:

(i) Guaranteed:

Life leases for which the resident is guaranteed a refund of 90% of the purchase price on vacating the unit are accounted for as life lease proceeds - guaranteed when the resident takes possession of the unit, except for the non-guaranteed 10%, which is recognized as revenue. Prior to possession, cash deposits and instalments paid are recorded as deposits on life leases.

(ii) Non-guaranteed:

Life leases for which the resident is not guaranteed any portion of their purchase price on vacating the unit are recognized as sales of the unit when the resident takes possession. Prior to possession, cash deposits and instalments paid are recorded as deposits on life leases.

2. Significant accounting policies (continued):

(j) Allocation of expenses:

The Army classifies expenses on the consolidated statement of operations by function. The Army allocates costs by identifying an appropriate basis of allocating and applying it on a consistent basis. When required, the Army allocates certain expenses on the following bases:

(i) Salaries and benefits are allocated based on the estimated hours worked within each function;

(ii) Occupancy costs are allocated based on the space occupied by each function; and

(iii) Administrative costs are allocated based on the estimated usage of each function.

(k) Use of estimates:

The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the year. Significant items subject to such estimates and assumptions include the useful lives of tangible capital assets, accrued liabilities, assets and obligations related to employee future benefits and allocation of expenses. Actual results could differ from those estimates.

3. Credit facilities:

The Army has Canadian dollar demand, revolving operating facilities ("lines of credit") with two Canadian banks for up to $7,000 (2016 - $7,000). The facilities are to cover Canadian and U.S. dollar overdrafts, as well as standby letters of credit. These lines of credit bear interest at the prime rate. At year end, the Army had not drawn on these lines of credit, other than to issue standby letters of credit in the amount of $607 (2016 - $607) (note 17(a)).

(In thousands of dollars)

4. Securities:

An analysis of the carrying value of securities is as follows:

	2017	2016
Cash and cash equivalents	$ 18,915	$ 16,041
Fixed income:		
Domestic	79,895	79,333
Foreign	2,848	1,572
Pooled funds:		
Fixed income:		
Domestic	112,125	141,440
Foreign	3,907	3,644
Equities	236,223	208,871
Equities:		
Domestic	208,476	208,113
Foreign	218,516	155,258
Real estate - domestic	80,654	76,232
Infrastructure - foreign	57,743	48,504
	$ 1,019,302	$ 939,008

Fixed income investments mature at various dates between August 2017 and October 2067 (2016 - May 2016 and October 2067), and bear interest at rates as follows:

	2017		2016	
Maturity	Low	High	Low	High
0 - 5 years	0.50%	8.75%	0.75%	8.75%
6 - 10 years	1.50%	9.92%	1.25%	9.92%
11 - 20 years	2.75%	7.60%	3.50%	8.50%
> 20 years	1.25%	6.10%	1.25%	6.75%

The carrying value of securities held in the General Investment Fund total $1,010,245 (2016 - $930,624), while $9,057 (2016 - $8,384) relates to other investment funds held by the Army.

5. Financial risks:

(a) Investment risk management:

Risk management relates to the understanding and active management of risks associated with all areas of the Army and the associated operating environment. Investments are primarily exposed to interest rate, market price and foreign currency risks. The Army has formal policies and procedures that establish a target asset mix. The Army's policies also require diversification of investments within categories, and set limits on exposure to individual investments.

(b) Interest rate risk:

Interest rate risk arises from the possibility that changes in interest rates will affect the value of fixed income securities held by the Army. This risk is managed by staggering the terms of the securities held, and ensuring diversification of the holdings, such that no single security, other than Government of Canada or provincial bonds, represents more than 5% of the fixed income component of the portfolio.

The Army is exposed to interest rate risk on the financing of 15 (2016 - 14) of its properties. The Army has entered into interest rate swaps with major Canadian banks to exchange the variable interest payments for fixed interest rates on all but one of its variable rate loans. Swap interest rates range from 2.00% to 6.27% (2016 - 2.00% to 6.27%). As at March 31, 2017, the swaps had a notional amount totaling $39,837 (2016 - $40,798) that reduces on a basis consistent with the repayment of principal of the underlying debt. The swaps mature between July 3, 2018 and October 19, 2026. By effectively converting the interest rates from variable to fixed, the Army has eliminated almost all the volatility, consistent with its interest rate risk management objectives. The one unhedged loan had a notional amount outstanding of $3,026 as at March 31, 2017 and an interest rate of 1.72%, tied to the one month bankers' acceptance CDOR rate. The Army monitors interest rates and may enter into an interest rate swap on this loan if interest rate risk increases.

(c) Market price risk:

Market price risk arises as a result of trading in equity securities and fixed income securities. Fluctuations in the market expose the Army to a risk of loss. The Army mitigates this risk through controls to monitor and limit concentration levels.

(In thousands of dollars)

5. Financial risks (continued):

(d) Foreign currency risk:

As at March 31, 2017, 28% (2016 - 22%) of the investments are invested in foreign securities.

Foreign currency risk arises from gains and losses due to fluctuations in foreign currency exchange rates on the Army's foreign securities. The Army does not hedge its foreign currency risk on these investments. The philosophy of the Army, and its global investment management service provider, is that since the portfolio is managed such that individual equities are held for the long term, and equities are held in multiple currencies, residual foreign exchange risk is considered acceptable in the long term without implementing a hedging strategy.

Within the fixed income component of the portfolio, the Army's statement of investment policies and procedures allows investment managers to hold a limited amount of non-Canadian dollar denominated bonds and when they do, to employ forward contracts to eliminate any related foreign currency risk.

6. Tangible capital assets:

			2017	2016
	Cost	Accumulated amortization	Net book value	Net book value
Land	$ 134,031	$ –	$ 134,031	$ 131,431
Buildings and land improvements	895,989	391,236	504,753	501,844
Furniture and equipment	52,024	34,862	17,162	13,987
Vehicles	13,495	10,287	3,208	3,018
Construction in progress	47,852	–	47,852	34,284
	$ 1,143,391	$ 436,385	$ 707,006	$ 684,564

As at March 31, 2017, the Army had assets held for sale with a net book value of $2,944 (2016 - $4,000).

(In thousands of dollars)

7. Other assets and liabilities:

(a) Other assets:

Included in other assets are charitable remainder trusts amounting to $3,411 (2016 - $3,411). A charitable remainder trust is an arrangement in which property or money is donated to a charity, but the donor continues to use the property and/or receive income from it while living.

(b) Other liabilities:

Other liabilities include gift annuities, which are planned giving arrangements, in the amount of $5,404 (2016 - $7,716).

8. Loans and mortgages payable:

Loans and mortgages payable are secured by either the investments or properties, bear interest at rates ranging from 0.00% to 9.63% (2016 - 0.00% to 9.63%) with an average interest rate of approximately 3.37% (2016 - 3.54%) and extend for terms of up to 27 years from March 31, 2017.

Some of these mortgages are subsidized by governments so that the effective interest rate to the Army is reduced.

Interest paid on loans and mortgages totals $2,979 (2016 - $3,475).

The aggregate amount of principal repayments required in each of the next five years and thereafter is as follows:

2018	$ 17,766
2019	13,833
2020	11,325
2021	20,151
2022	4,391
Thereafter	19,138
	86,604
Less current portion	17,766
	$ 68,838

(In thousands of dollars)

9. Employee future benefits:

(a) Officers' retirement benefits:

2017	Defined benefit pension plan	Supplementary retirement pension	Other retirement benefit plans	Total employee future benefits
Accrued benefit obligation	$ 216,579	$ 22,340	$ 116,064	$ 354,983
Fair value of plan assets	198,997	–	–	198,997
Plan deficit	$ 17,582	$ 22,340	$ 116,064	$ 155,986

2016	Defined benefit pension plan	Supplementary retirement pension	Other retirement benefit plans	Total employee future benefits
Accrued benefit obligation	$ 210,005	$ 22,940	$ 112,722	$ 345,667
Fair value of plan assets	181,300	–	–	181,300
Plan deficit	$ 28,705	$ 22,940	$ 112,722	$ 164,367

Continuity of the employee future benefits liability is as follows:

	Defined benefit pension plan	Supplementary retirement pension	Other retirement benefit plans	2017	2016
Balance, beginning of year	$ 28,705	$ 22,940	$ 112,722	$ 164,367	$ 168,013
Benefit expense	6,005	932	5,678	12,615	13,546
Employer contributions	(2,973)	(1,742)	(4,552)	(9,267)	(8,691)
Remeasurement and other items	(14,155)	210	2,216	(11,729)	(8,501)
Balance, end of year	$ 17,582	$ 22,340	$ 116,064	$ 155,986	$ 164,367

Remeasurements and other items include the difference between the actual return on plan assets and the return calculated using the discount rate used to determine the defined benefit obligation and actuarial gains and losses.

(In thousands of dollars)

9. Employee future benefits (continued):

The Army's net benefit plan expenses are as follows:

2017	Defined benefit pension plan	Supplementary retirement pension	Other retirement benefit plans	Total
Current service cost	$ 4,799	$ 90	$ 1,418	$ 6,307
Interest cost	1,206	842	4,260	6,308
	$ 6,005	$ 932	$ 5,678	$ 12,615

2016	Defined benefit pension plan	Supplementary retirement pension	Other retirement benefit plans	Total
Current service cost	$ 5,210	$ 89	$ 2,149	$ 7,448
Interest cost	882	825	4,391	6,098
	$ 6,092	$ 914	$ 6,540	$ 13,546

Additional expenses for officers' benefits, consisting of cash payments made by the Army directly to beneficiaries for its unfunded other retirement benefit plans and other current benefits for the active officers were $3,142 (2016 - $2,914).

The Army measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at March 31 of each year. The most recent actuarial valuation for funding purposes of the pension plan and other retirement benefit plans was as at March 31, 2014 and March 31, 2015, respectively. The next actuarial valuations for both plans will be as at March 31, 2017 and are not yet available.

(In thousands of dollars)

9. Employee future benefits (continued):

(b) Pre-retirement benefits:

Included in other liabilities are accrued pre-retirement benefits of $3,461 (2016 - $3,446), representing health and sick leave future payments for certain ministry units.

(c) Employees' retirement benefits:

The contributions paid and expensed by the Army for the year amounted to $17,214 (2016 - $15,929). The assets of the employees' retirement benefits plan are held separately from those of the Army in an independently administered fund.

(d) Multi-employer defined benefit plans:

Several ministry units are part of multi-employer defined benefit plans under which contributions are made by the individual ministry units. For the fiscal year ended March 31, 2017, contributions paid and expensed in the amount of $3,900 (2016 - $3,802) are included in charitable programs and services.

10. Deposits on life leases:

	2017	2016
Balance, beginning of year	$ 12,155	$ 12,237
Amounts reclassified from deposits on life lease upon occupancy	838	1,000
Current year activity:		
Refunds	(1,104)	(984)
Amounts recognized as revenue	(84)	(98)
Balance, end of year	$ 11,805	$ 12,155

Under some life lease contracts signed to date, GCC has committed to the life occupancy resident that upon termination of the resident's life lease, GCC will attempt to lease the unit and reimburse the resident from the proceeds. However, as a minimum, GCC has guaranteed that the resident will receive not less than 90% of the original amount of the life lease proceeds. While repayment of these life lease proceeds could be required at any time, in the opinion of management, it is unlikely that material amounts of such repayments will be required in the next year.

(In thousands of dollars)

11. Fund balances:

(a) The Operating Fund balance consists of $103,694 (2016 - $103,635) held for normal operations, which includes the cumulative translation adjustment of $4,676 (2016 - $4,326) arising from the currency translation of self-sustaining operations in Bermuda, and ($73,979) (2016 - ($104,508)) related to remeasurement of the value of employee future benefits. The Army has a plan to fund the remeasurement deficit over the average remaining service life of the employees concerned, which is estimated at 12.3 years (2016 - 10.9 years). In 2017, $18,800 was applied to the shortfall (2016 - $2,800).

(b) The Endowment Fund balance is restricted as follows:

2017	Externally restricted	Internally restricted	Total
Ministry units	$ 8,184	$ 1,930	$ 10,114
DHQ	4,836	3,072	7,908
THQ	19,375	26,052	45,427
	$ 32,395	$ 31,054	$ 63,449

2016	Externally restricted	Internally restricted	Total
Ministry units	$ 8,184	$ 1,930	$ 10,114
DHQ	4,668	8,185	12,853
THQ	19,131	20,878	40,009
	$ 31,983	$ 30,993	$ 62,976

(c) The Other Restricted Funds balance is restricted as follows:

2017	Externally restricted	Internally restricted	Total
Ministry units	$ 28,190	$ 120,219	$ 148,409
DHQ	98,048	94,308	192,356
THQ	51,102	405,562	456,664
	$ 177,340	$ 620,089	$ 797,429

(In thousands of dollars)

11. Fund balances (continued):

2016		Externally restricted		Internally restricted		Total
Ministry units	$	37,136	$	111,839	$	148,975
DHQ		90,096		67,748		157,844
THQ		53,725		342,737		396,462
	$	180,957	$	522,324	$	703,281

As described in note 1(b)(ii), the Army mitigates the impact of the inherent volatility in capital markets on its operations by planning its spending based on a long-term expected rate of return rather than the actual investment earnings recognized in a particular year. As a result, the Army maintains a reserve with a target balance between 25% and 33% of the fair market value of its investments portfolio. The balance of this internally restricted reserve held in the Other Restricted Funds was $360,001 (2016 - $269,900) and represents funds held for future operations in years when actual earnings are below the long-term expected rate of return. The General Investment Fund (note 4) was valued at $1,010,245 (2016 - $930,624), meaning the reserve balance represents 36% (2016 - 29%) of the market value. The Army will review the excess reserve that exists during the year to determine if funds will be released to bring the balance down to the targeted level.

12. Investment income (loss):

		2017		2016
Interest	$	9,196	$	11,845
Dividends		17,373		13,524
Net realized gains on sale of securities		32,067		49,372
Change in net unrealized gain (loss) on securities		68,139		(97,129)
	$	126,775	$	(22,388)

(In thousands of dollars)

13. Expenses by category:

Expenses comprise the following categories:

	2017	2016
Salaries and benefits	$ 431,531	$ 419,340
Other program and general operating	153,788	145,062
Occupancy	85,275	93,046
Amortization	30,482	30,206
	$ 701,076	$ 687,654

14. Net interfund transfers:

2017	Operating Fund	Endowment Fund	Other Restricted Funds	Capital Fund
Funding of operations from reserves	$ 130,362	$ –	$ (130,362)	$ –
Funding of capital transactions from operations and reserves	(18,183)	–	(26,023)	44,206
Transfers from internally restricted endowment to reserves	–	(5,113)	5,113	–
Net transfer to internally restricted reserves	(3,588)	5,165	(1,577)	–
Transfer of property sale proceeds	1,265	–	32,224	(33,489)
Transfers for future property repairs/maintenance	(7,820)	–	7,820	–
Net investment gain transferred from reserve for future operations (notes 1(b)(ii) and 11(c))	(119,544)	–	119,544	–
Unrestricted legacies transferred to reserve for future operations	(21,841)	–	21,841	–
Other	(635)	128	609	(102)
	$ (39,984)	$ 180	$ 29,189	$ 10,615

(In thousands of dollars)

14. Net interfund transfers (continued):

2016	Operating Fund	Endowment Fund	Other Restricted Funds	Capital Fund
Funding of operations from reserves	$ 111,629	$ –	$ (111,629)	$ –
Funding of capital transactions from operations	(3,369)	–	–	3,369
Transfers from internally restricted endowment to reserves	–	(3,578)	3,578	–
Transfer to internally restricted reserves	(17,596)	–	17,596	–
Transfer of property sale proceeds	7,387	–	13,812	(21,199)
Transfers for future property repairs/maintenance	(13,887)	–	13,887	–
Net investment loss funded from reserve (notes 1(b)(ii) and 11(c))	24,762	–	(24,762)	–
Unrestricted legacies transferred to reserve for future operations	(18,083)	–	18,083	–
Other	1,867	–	(1,857)	(10)
	$ 92,710	$ (3,578)	$ (71,292)	$ (17,840)

15. Consolidated statement of cash flows:

(a) Items not affecting cash:

	2017	2016
Gain on disposal of tangible capital assets	$ (24,293)	$ (15,972)
Amortization	30,482	30,206
Increase (decrease) in pre-retirement benefits	15	(30)
Other retirement benefits expense	5,678	6,540
Defined benefit and supplementary retirement pension plan expense	6,937	7,006
Net realized gains on sale of securities	(32,067)	(49,372)
Change in net unrealized loss (gain) on securities	(68,139)	97,129
	$ (81,387)	$ 75,507

(In thousands of dollars)

15. Consolidated statement of cash flows (continued):

(b) Change in non-cash operating working capital:

	2017	2016
Receivables and other current assets	$ 4,671	$ (4,161)
Accounts payable and accrued liabilities	(5,186)	4,516
Deferred revenue	(48)	674
	$ (563)	$ 1,029

16. Lease commitments:

The Army has lease commitments for premises used in its operations. These leases expire on or before 2057. The lease payments are due as follows:

2018	$ 19,063
2019	14,604
2020	11,392
2021	7,097
2022	4,427
Thereafter	9,693
	$ 66,276

17. Contingencies and commitments:

(a) Letters of credit and letters of comfort:

The Army enters into agreements in the normal course of operations that contain features which meet the definition of a guarantee, according to the CPA Canada Handbook. Various debt obligations (such as overdrafts and lines of credit) related to certain ministry units have been directly guaranteed by The Governing Council. No material loss is anticipated by reason of such agreements and guarantees.

As at March 31, 2017, the Army had issued letters of credit totaling $607 (2016 - $607). These are primarily irrevocable standby letters of credit issued in favour of municipalities and other entities requiring performance guarantees on projects undertaken by the Army.

17. Contingencies and commitments (continued):

(b) Contingent liabilities:

The Army receives government assistance in the form of forgivable loans to fund some capital projects. This funding is considered a grant as long as the Army continues to meet the terms of the agreements. In the event of default, the funding is repayable to the government. As at year end, the Army has an unforgiven loan balance of $30,703 (2016 - $30,998) of such funding. Management believes that it is currently in compliance with all such agreements and, accordingly, no amounts are recorded as a liability in these consolidated financial statements related to this assistance.

(c) Government capital contribution for a program:

In fiscal 2010, the Army acquired title to a property in Milton, Ontario from the Province of Ontario as part of an agreement to operate a program for young offenders. Under the agreement, the province retains the right to reacquire the property, valued at $4,440 at the time of acquisition, under certain conditions, such as if the Army ceases to operate the program. The Army intends to operate the program for the foreseeable future and meet all conditions set by the province for its operations; as a result, the transfer of property has been reflected in these consolidated financial statements as an increase in tangible capital assets and by recognizing revenue in the form of capital contributions.

(d) Legal actions:

The Army is party to legal actions arising in the ordinary course of operations. While it is not feasible to predict the outcome of these actions, it is the opinion of management that the resolution of these matters will not have a material adverse effect on the operations of the Army.

(e) Indemnification of directors and officers:

The Army has indemnified, its past, present and future members of The Governing Council, directors of controlled corporations, officers, trustees, employees and volunteers against expenses (including legal expenses), judgments and any amount actually or reasonably incurred by them in connection with any actual or alleged wrongful act in which the directors are sued as a result of their service, if they acted honestly and in good faith with a view of the best interests of the Army. The nature of the indemnity prevents the Army from reasonably estimating the maximum exposure. The Army has purchased liability insurance with respect to this indemnification.

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