

Financial Statements of

**MICHAEL SMITH FOUNDATION
FOR HEALTH RESEARCH**

Years ended March 31, 2004 and 2003



KPMG LLP
Chartered Accountants
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Canada

AUDITORS' REPORT

To the Members of the
Michael Smith Foundation for Health Research

We have audited the statement of financial position of Michael Smith Foundation for Health Research as at March 31, 2004 and the statements of operations, changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Foundation's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Foundation as at March 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the Society Act (British Columbia), we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

KPMG LLP

Chartered Accountants

Vancouver, Canada

April 30, 2004



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MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statements of Financial Position

March 31, 2004 and 2003

	2004	2003
Assets		
Current assets:		
Cash	\$ 41,120,812	\$ 9,782,378
Short-term investments (note 3)	27,022,108	21,211,845
Accounts receivable	92,968	220,015
Prepaid expenses and deposits	14,051	5,032
	<u>68,249,939</u>	<u>31,219,270</u>
Long-term investments (note 3)	42,002,820	69,598,315
Endowment funds (note 3)	2,233,539	3,619,610
Capital assets (note 4)	881,902	590,168
	<u>\$113,368,200</u>	<u>\$ 105,027,363</u>

Liabilities and Net Assets

Current liabilities:		
Accounts payable and accrued liabilities	\$ 774,293	\$ 563,309
Grants payable	419,885	619,927
	<u>1,194,178</u>	<u>1,183,236</u>
Deferred contributions (note 5):		
Contributions for expenses of future periods	90,591,173	91,634,349
Capital contributions	881,902	590,168
Restricted projects	18,467,408	8,000,000
	<u>109,940,483</u>	<u>100,224,517</u>
Net assets:		
Restricted for endowment purposes (note 3)	2,233,539	3,619,610
	<u>\$ 113,368,200</u>	<u>\$ 105,027,363</u>


Commitments (note 6)

See accompanying notes to financial statements.

Approved on behalf of the Foundation:



Director



Director

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statements of Operations

	Year ended March 31, 2004	Year ended March 31, 2003
Revenues:		
Amortization of deferred contributions (note 5(a))	\$ 20,972,315	\$ 17,582,332
Amortization of deferred capital contributions (note 5(b))	206,457	146,896
Restricted projects (note 5(c))	1,428,510	968,020
Other	266,693	74,977
	<u>22,873,975</u>	<u>18,772,225</u>
Expenses:		
Grants and awards:		
Career	8,545,411	6,007,099
Trainee	2,848,980	2,154,380
Canadian Institute for Health Research training centres	75,000	1,713,775
British Columbia Health Research Foundation scholars and trainees	89,685	290,702
Research Institutions	2,810,849	235,406
Research Units	2,150,945	225,000
Genome BC	-	3,650,000
Other grants-in-aid	100,000	20,000
Program development and delivery	1,381,921	1,012,030
Coordination, research and analysis	310,901	133,899
Restricted project expenses (note 5(c))	1,428,510	968,020
	<u>19,742,202</u>	<u>16,410,311</u>
Administration:		
General operating	2,217,881	1,904,728
Information services	707,435	310,290
Amortization of capital assets	206,457	146,896
	<u>3,131,773</u>	<u>2,361,914</u>
	<u>22,873,975</u>	<u>18,772,225</u>
Excess of revenues over expenses	\$ -	\$ -

See accompanying notes to financial statements.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statements of Changes in Net Assets

	Restricted for Endowment	Unrestricted	Year ended March 31, 2004	Year ended March 31, 2003
Balance, beginning of year	\$ 3,619,610	\$ -	\$ 3,619,610	\$ -
Transfer of endowment funds from British Columbia Health Research Foundation (note 7)	-	-	-	3,619,610
Transfer of endowment funds to Vancouver Foundation (note 3)	(1,386,071)	-	(1,386,071)	-
Balance, end of year	\$ 2,233,539	\$ -	\$ 2,233,539	\$ 3,619,610

See accompanying notes to financial statements.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statements of Cash Flows

	Year ended March 31, 2004	Year ended March 31, 2003
Cash flows from operating activities:		
Contributions from the Province of British Columbia - operations	\$ 15,000,000	\$ -
Contributions from the Province of British Columbia - Restricted projects	11,870,000	8,000,000
Contributions from the Province of Manitoba - Restricted projects	25,918	-
Contributions from Western Economic Diversification - Restricted projects	-	906,063
Grants and awards	(16,820,912)	(16,756,372)
Program development, delivery and administration	(4,406,681)	(3,255,857)
Restricted project expenses	(1,310,955)	(800,575)
Other revenue	266,693	74,977
Gain on sale of equities	1,805,615	-
Investment revenue	3,661,208	3,913,895
	10,090,886	(7,917,869)
Cash flows from investing activities:		
Change in short-term investments	(5,810,263)	13,228,222
Change in long-term investments	27,595,495	4,283,754
Change in endowment investments	1,386,071	(3,619,610)
Purchase of capital assets	(498,191)	(151,329)
	22,673,112	13,741,037
Cash flows from financing activities:		
Dissolution of British Columbia Health Research Foundation (note 7)	-	3,924,635
Transfer of endowment (note 3)	(1,425,564)	-
	(1,425,564)	3,924,635
Increase in cash	31,338,434	9,747,803
Cash, beginning of year	9,782,378	34,575
Cash, end of year	\$ 41,120,812	\$ 9,782,378

See accompanying notes to financial statements.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

1. Nature of operations:

The Michael Smith Foundation for Health Research (the "Foundation") was incorporated on March 7, 2001 under the Society Act (British Columbia). The Foundation is a registered charity under the Income Tax Act (the "Act") and accordingly is exempt from income and capital taxes and is able to issue donation receipts for income tax purposes.

The Foundation was established to create a vibrant and sustainable British Columbian health research environment that is recognized for excellence and:

- has the human resources, infrastructure and research space to compete effectively for national and international funding across all sectors;
- anticipates and responds to B.C. health needs;
- builds the B.C. economy; and
- networks for critical mass across Western Canada, nationally and internationally.

At its inception, the Foundation received a \$110 million grant from the Province of British Columbia based on the vision included in a comprehensive five-year plan developed by a coalition representing the broad health research community in British Columbia. Each year the Foundation conducts a range of peer-reviewed grant programs that draw down on this initial grant. The Foundation also receives additional funding from the Province of British Columbia and other sources to undertake various projects consistent with its purpose.

2. Significant accounting policies:

(a) Basis of accounting:

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles for not-for-profit organizations. The Foundation follows the deferral method of accounting for contributions that include grants, donations and service contracts from other sources.

(b) Capital assets:

Capital assets are recorded at cost less accumulated amortization. Leasehold improvements are amortized on a straight-line basis over the term of the lease. Other capital assets are amortized on a straight-line basis over their estimated useful life at the following annual rates:

Asset	Rate
Furniture	20%
Office equipment	20%
Computer equipment	30%
Computer software	100%

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

2. Significant accounting policies (continued):

(c) Short-term investments:

Short-term investments include term deposits, banker's acceptances, bonds, and commercial paper with a term to maturity of less than one year, and are carried at the lower of cost and market value.

(d) Long-term investments:

Long-term investments include term deposits, banker's acceptances, bonds, commercial paper, and securities with a term to maturity of more than one year, and are carried at cost less provision for permanent declines in market value.

(e) Revenue recognition:

In March 2001, the provincial government of British Columbia provided a grant of \$110 million to establish the Foundation and implement a five-year strategic plan. Under the terms of the Foundation's bylaws, this funding, along with the future investment income, will be directed to the granting of funds to eligible recipients and the payment of the Foundation's operating and capital expenditures. This restricted contribution, along with any additional related grants and the investment income thereon, are deferred and recognized as revenue in the year in which the related expenses are incurred by the Foundation.

The Foundation also receives various other restricted contributions through project grants or contracts that are deferred and recognized as revenue in the year in which the related expenses are incurred by the Foundation. Endowment contributions are recorded as a direct increase in net assets. Investment income earned on endowment contributions are deferred and recognized as revenue in the year in which the related expenses are incurred by the Foundation.

Restricted contributions applied toward the purchase of capital assets are deferred and amortized to revenue, at a rate corresponding with the amortization rate for the related capital assets.

From time to time the Foundation's Board of Directors may place internal restrictions on certain endowments or other resources such that the resources are available only for the specified purpose.

Unrestricted contributions are recognized as revenue in the current period if the amount to be received can be reasonably estimated and collection is reasonably assured. Unrestricted investment and other income are recognized as revenue when earned.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

2. Significant accounting policies (continued):

(f) Grants and awards:

Grants and awards approved by the Foundation are recorded as expenses in the fiscal year that the payment is to be made. Amounts are usually paid in quarterly installments in advance.

(g) Volunteer services:

The Foundation gratefully acknowledges the significant contribution it receives in the form of services from a large number of volunteer peer reviewers, committee members and task force participants. Such services, while essential to the Foundation's operations, are not recorded in these financial statements because of the difficulty of assigning a particular value to them.

(h) Lease inducement:

Cash payments received as lease inducements by the Foundation under the terms of the lease for office premises are being amortized to income through a reduction of rental expense over the term of the lease. The unamortized balance of \$208,049 (2003 - \$132,210) has been included in accounts payable and accrued liabilities.

3. Investments:

	2004	2003
Bonds and other investments	\$ 70,650,923	\$ 86,637,056
Equities	607,544	7,792,714
Total investments	71,258,467	94,429,770
Short-term	27,022,108	21,211,845
Endowment funds	2,233,539	3,619,610
Long-term	\$ 42,002,820	\$ 69,598,315

Investments have maturity dates ranging from fiscal 2004 to fiscal 2008.

The investments, with a book value of \$71,258,467, have a market value of \$72,967,866.

During the year, the Foundation received Court approval to transfer contributions restricted for endowment purposes to the Vancouver Foundation with a book value of \$1,386,071, together with accumulated unspent investment income of \$39,493. The transfer was completed on January 28, 2004.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

4. Capital assets:

2004	Cost	Accumulated amortization	Net book value
Computer software	\$ 116,716	\$ 95,251	\$ 21,465
Computer hardware	257,854	84,404	173,450
Office furniture	420,911	152,437	268,474
Leasehold improvements	507,839	89,326	418,513
	\$ 1,303,320	\$ 421,418	\$ 881,902

2003	Cost	Accumulated amortization	Net book value
Computer software	\$ 73,786	\$ 57,719	\$ 16,067
Computer hardware	112,263	28,886	83,377
Office furniture	299,409	80,405	219,004
Leasehold improvements	319,671	47,951	271,720
	\$ 805,129	\$ 214,961	\$ 590,168

5. Deferred contributions:

Deferred contributions represent unspent grants or contract resources restricted for specific purposes such as undertaking the five year strategic plan or other restricted projects, and include expenses for operating as well as capital purposes.

(a) Deferred contributions relating to expenses of future periods:

	2004	2003
Balance, beginning of year	\$ 91,634,349	\$ 105,359,462
Contributions received during the year:		
Grant from Province of British Columbia	15,000,000	-
Gain on sale of equities	1,805,615	-
Investment income earned during the year	3,661,208	3,913,895
Investment income transferred from BCHRF (note 7)	-	71,709
	112,101,172	109,345,066
Amounts recognized as revenue during the period	(20,972,315)	(17,582,332)
Amounts applied toward capital assets purchased during the period	(498,191)	(128,385)
Investment income transferred to Vancouver Foundation (note 3)	(39,493)	-
Balance, end of year	\$ 90,591,173	\$ 91,634,349

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

5. Deferred contributions (continued):

(a) Deferred contributions relating to expenses of future periods (continued):

The \$15 million grant received during the year from the Province of British Columbia is to be used to fund programs in British Columbia which continue to develop, attract and retain outstanding health scientists and researchers.

(b) Deferred contributions relating to capital assets:

	2004	2003
Balance, beginning of year	\$ 590,168	\$ 585,735
Allocation of deferred contributions - operations (note 5(a))	498,191	128,385
Restricted project - Western Economic Diversification	-	22,944
Amounts amortized to revenue	(206,457)	(146,896)
Balance, end of year	\$ 881,902	\$ 590,168

(c) Restricted projects:

	2004	2003
Balance, beginning of year	\$ 8,000,000	\$ -
Restricted projects - Province of British Columbia	11,870,000	8,000,000
Restricted project - Province of Manitoba	25,918	-
Restricted project - Western Economic Diversification	-	968,020
	19,895,918	8,968,020
Amounts amortized to revenue	(1,428,510)	(968,020)
Balance, end of year	\$ 18,467,408	\$ 8,000,000

The \$11,870,000 received from the Province of British Columbia in 2004 consisted of:

- Health services and policy research - \$8,000,000
- Academic emergency medicine research - \$1,270,000
- SARS vaccine research - \$2,600,000.

During the year, the Foundation also received \$25,918 from the Province of Manitoba for research related to Fetal Alcohol Spectrum Disorder (FASD). The project was completed during the year.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

5. Deferred contributions (continued):

(c) Restricted projects (continued):

The balance of deferred contributions for restricted contributions is comprised of the following:

	2004	2003
Health services and policy research	\$ 15,965,219	\$ 8,000,000
Academic emergency medicine research	1,270,000	-
SARS vaccine research	1,232,189	-
	<u>\$ 18,467,408</u>	<u>\$ 8,000,000</u>

6. Commitments:

(a) Grant commitments:

Through a variety of targeted granting programs, the Foundation commits the majority of its funds to providing peer-reviewed research awards aimed at fulfilling the Foundation's mandate. Many of the commitments made through these granting programs have terms that span more than one fiscal year.

The following table summarizes commitments approved by the Foundation, by major grant program.

Grant program	Commitments for the years ending March 31		Total
	2005	2006 and thereafter	
Career	\$ 7,901,397	\$ 7,610,316	\$ 15,511,713
Trainee	2,332,562	1,315,752	3,648,314
CIHR training centres	75,000	68,750	143,750
BCHRF scholars and trainees	13,680	-	13,680
Research Institutions	3,747,795	3,747,795	7,495,590
Research Units	2,877,566	2,877,566	5,755,132
	<u>\$ 16,948,000</u>	<u>\$ 15,620,179</u>	<u>\$ 32,568,179</u>

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Years ended March 31, 2004 and 2003

6. Commitments (continued):

(b) Office space and equipment lease commitments:

The Foundation rents office space under a long-term lease, which expires July 31, 2011 and provides for an additional 5 year extension at the option of the Foundation. During the year the Foundation leased additional office space adjacent to its existing premises which also expire July 31, 2011, with a five year extension at the option of the Foundation.

During the year, the Foundation also leased office space related to restricted project activities at \$2,000 per month ending December 3, 2004.

The Foundation also leases various office equipment.

The Foundation has future minimum lease payments under operating leases as follows:

Year ending March 31:

2005	\$ 388,160
2006	368,440
2007	377,726
2008	347,786
2009 and thereafter	1,103,980
	<hr/>
	\$ 2,586,092

7. Related party transactions:

On July 11, 2002, British Columbia Order in Council – Deregulation Statutes Amendment Act (No. 2) 2002, was approved by the Province of British Columbia. This Order dissolved the British Columbia Health Research Foundation (“BCHRF”) and transferred all of the assets and liabilities of BCHRF to the Foundation.

The Foundation agreed to assume responsibility for the costs associated with any renewal of the BCHRF’s existing scholar and trainee awards. The total paid in the period for BCHRF renewal grants was \$89,685 (2003 - \$290,702). The anticipated future cost to complete these renewal grants by June 2004 is \$13,680 (2003 - \$142,430). These amounts are included in the expenses of the Foundation or in the commitments summarized in note 6, respectively.