

Financial Statements of

**MICHAEL SMITH FOUNDATION FOR
HEALTH RESEARCH**

Year ended March 31, 2014



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INDEPENDENT AUDITORS' REPORT

To the Members of the
Michael Smith Foundation for Health Research

Report on the Financial Statements

We have audited the accompanying financial statements of Michael Smith Foundation for Health Research, which comprise the statement of financial position as at March 31, 2014, the statements of operations and cash flows for the year ended March 31, 2014, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian accounting standards for not-for-profit organizations, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Michael Smith Foundation for Health Research as at March 31, 2014 and its result of operations and its cash flows for the year ended March 31, 2014 in accordance with Canadian accounting standards for not-for-profit organizations.



Report on Other Legal and Regulatory Requirements

As required by the Society Act (British Columbia), we report that, in our opinion, the accounting policies applied in preparing and presenting the financial statements in accordance with the Canadian accounting standards for not-for-profit organizations have been applied on a basis consistent with that of the preceding year.

A handwritten signature in black ink that reads 'KPMG LLP'. The signature is written in a cursive, slightly slanted style. Below the signature is a long, horizontal, slightly curved line that serves as a flourish or underline.

Chartered Accountants

July 11, 2014

Burnaby, Canada

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statement of Financial Position

March 31, 2014, with comparative information for 2013

	2014	2013
Assets		
Current assets:		
Cash	\$ 1,843,482	\$ 939,320
Contributions and other amounts receivable	15,111,775	22,964,378
Short-term investments (note 3)	62,123,927	58,557,724
Prepaid expenses and deposits	100,105	92,462
	<u>79,179,289</u>	<u>82,553,884</u>
Long-term investments (note 3)	3,013,992	2,905,309
Capital assets (note 4)	92,622	56,332
	<u>\$ 82,285,903</u>	<u>\$ 85,515,525</u>

Liabilities and Net Assets

Current liabilities:		
Accounts payable and accrued liabilities (note 5)	\$ 479,265	\$ 532,820
Grants payable	-	16,742
	<u>479,265</u>	<u>549,562</u>
Deferred contributions (note 6):		
Contributions for expenses of future periods	64,193,758	66,576,146
Capital contributions	92,622	56,332
Sponsored projects	15,253,719	16,066,946
	<u>79,540,099</u>	<u>82,699,424</u>
Net assets:		
Restricted for endowment purposes	2,266,539	2,266,539
Commitments (note 7)		
	<u>\$ 82,285,903</u>	<u>\$ 85,515,525</u>

See accompanying notes to financial statements.

Approved on behalf of the Foundation:



Director



Director

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statement of Operations

Year ended March 31, 2014, with comparative information for 2013

	2014	2013
Revenue:		
Contributions recognized in current year (note 6(a))	\$ 15,145,879	\$ 16,608,640
Contributions recognized in current year – sponsored projects (note 6(c))	4,316,557	3,646,281
Amortization of deferred capital contributions (note 6(b))	41,244	73,300
Other	525,051	566,261
	<u>20,028,731</u>	<u>20,894,482</u>
Expenses:		
Programs and projects		
Career	6,185,835	8,269,038
Trainee	1,638,696	1,485,019
Research networks	700,000	642,305
Monitoring, evaluation, and learning system	1,433,161	1,351,681
Knowledge translation	227,409	257,986
Ethics harmonization	166,750	282,248
BC Influenza Vaccine	33,334	-
Other	378,458	155,333
Program and project delivery	1,610,053	1,035,617
Sponsored project expenses (note 6(c))	4,316,557	3,646,281
	<u>16,690,253</u>	<u>17,125,508</u>
Administration:		
General operating	3,297,234	3,695,674
Amortization of capital assets	41,244	73,300
	<u>3,338,478</u>	<u>3,768,974</u>
	<u>20,028,731</u>	<u>20,894,482</u>
Excess of revenue over expenses	\$ -	\$ -

See accompanying notes to financial statements.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Statement of Cash Flows

Year ended March 31, 2014, with comparative information for 2013

	2014	2013
Cash flows from operating activities:		
Contributions from the Province of British Columbia		
Operations	\$ 20,000,000	\$ 41,000,000
Sponsored projects	2,700,000	1,500,000
Grants and awards	(10,620,210)	(12,624,882)
Program and project delivery and administration	(4,982,082)	(4,982,721)
Sponsored project expenses	(4,408,890)	(3,648,099)
Other revenue	525,051	566,260
Investment revenue	1,342,335	2,171,227
Net cash provided by (used in) operating activities	4,556,204	23,981,785
Cash flows from investing activities:		
Purchase of investments	(37,497,987)	(183,788,587)
Proceeds from sale of investments	33,923,479	156,041,696
Purchase of capital assets (note 6(a))	(77,534)	(32,468)
Net cash provided by (used in) investing activities	(3,652,042)	(27,779,359)
Net increase (decrease) in cash	904,162	(3,797,574)
Cash, beginning of year	939,320	4,736,894
Cash, end of year	\$ 1,843,482	\$ 939,320

The Foundation uses the direct method in preparation of its statement of cash flows.

See accompanying notes to financial statements.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements

Year ended March 31, 2014

1. Nature of operations:

The Michael Smith Foundation for Health Research (the "Foundation") is incorporated under the Society Act (British Columbia) and is a registered charity under the Income Tax Act. Accordingly the Foundation 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 and health system needs;
- builds the B.C. economy; and
- networks for critical mass across Western Canada, nationally and internationally.

The Foundation receives funding from the Province of British Columbia to conduct a range of peer-reviewed grant programs and other projects. In addition, the Foundation receives funding from other sources to undertake various projects consistent with its purpose.

2. Significant accounting policies:

(a) Basis of accounting:

The financial statements have been prepared in accordance with Canadian accounting standards for not-for-profit organizations in Part III of the Canadian Institute of Chartered Accountants (CICA) Handbook.

(b) Revenue recognition:

The Foundation follows the deferral method of accounting for contributions, including grants and donations from other sources.

Funding received from the Province of British Columbia, along with the future investment income, will be directed to the granting of funds to eligible recipients, the support of strategic initiatives and the payment of the Foundation's operating and capital expenditures. These restricted contributions, 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. Restricted contributions used for the purchase of capital assets are deferred and amortized to revenue at a rate corresponding with the amortization rate for the related capital assets.

The Foundation also receives various other restricted contributions through sponsored project grants, contracts or matching contributions from other organizations that are deferred and recognized as revenue in the year in which the related expenses are incurred by the Foundation.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

2. Significant accounting policies (continued):

(b) Revenue recognition (continued):

Endowment contributions are recorded as a direct increase in net assets. Realized and unrealized investment income earned on endowment investments is deferred and recognized as revenue in the year in which the related expenses are incurred by the Foundation.

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 income is recognized as revenue when earned.

(c) Capital assets:

Capital assets are recorded at cost less accumulated amortization. Repairs and maintenance costs are charged to expense. Capital assets are amortized on a straight-line basis over their estimated useful lives as follows:

Asset	Period
Computer software	1 year
Computer hardware	3 years
Office furniture	5 years
Office equipment	5 years

(d) Intangible assets:

Costs related to internally generated intangible assets during the development phase are recorded as an expense as they are incurred.

(e) Financial instruments:

Financial instruments are initially measured at fair value. Subsequently, equity instruments quoted in an active market are measured at fair value. Other instruments are subsequently measured at amortized cost unless elected to be measured at fair value. The Foundation has elected to carry its investments at fair value.

Transaction costs incurred on the acquisition of financial instruments measured subsequently at fair value 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.

Financial assets measured at amortized cost are assessed for impairment on an annual basis at the end of the fiscal year if there are indicators of impairment. If there is an indicator of impairment, the Foundation 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 Foundation expects to realize by exercising its right to any collateral. If events and circumstances reverse in a future period, an impairment loss will be reversed to the extent of the improvement, not exceeding the initial carrying value.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

2. Significant accounting policies (continued):

(e) Financial instruments (continued):

The Foundation's financial instruments consist of cash, contributions and other amounts receivable, short and long term investments, accounts payable and accrued liabilities and grants payable.

Contributions and other amounts receivable

- (i) Contributions and other amounts receivable are measured at amortized cost using the effective interest method and approximate their fair values due to the relatively short periods to maturity.

Investments

- (i) Short-term investments - include any term deposits, guaranteed investment certificates, treasury bills, bankers' acceptances, income funds, bonds or equities, with a term to maturity of less than one year. Short-term investments are measured at fair value with subsequent changes to fair value recorded as changes in deferred contributions and recognized as revenues when the related expenses are incurred.
- (ii) Long-term investments - include any term deposits, guaranteed investment certificates, treasury bills, bankers' acceptances, bonds, commercial paper and equities with a term to maturity of more than one year or that are related to permanent endowments. Long-term investments are measured at fair value with subsequent changes in fair value recorded as changes in deferred contributions and recognized as revenues when the related expenses are incurred.

Financial Liabilities

- (i) Accounts payable, grants payable and accrued liabilities are measured at amortized cost using the effective interest method.

(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 determining their fair value.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

2. Significant accounting policies (continued):

(h) Use of estimates:

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

3. Investments:

	2014	2013
Income funds	\$ 30,176,129	\$ 45,217,718
Term deposits	31,596,822	13,492,406
Equities	3,364,968	2,752,909
Total investments	65,137,919	61,463,033
Short-term	62,123,927	58,557,724
Long-term	\$ 3,013,992	\$ 2,905,309

Investments in term deposits mature in fiscal 2015. Investments related to endowments are classified as long-term.

4. Capital assets:

			2014	2013
	Cost	Accumulated amortization	Net book value	Net book value
Computer software	\$ 639,987	\$ 632,305	\$ 7,682	\$ 3,913
Computer hardware	473,198	406,726	66,472	22,222
Office furniture and equipment	562,711	544,243	18,468	30,197
Leasehold improvements	632,224	632,224	-	-
	\$ 2,308,120	\$ 2,215,498	\$ 92,622	\$ 56,332

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

5. Accounts payable and accrued liabilities:

Included in accounts payable are government remittances payable of nil (2013 - \$11,282).

6. Deferred contributions:

Deferred contributions represent unspent grants or contract resources restricted for specific purposes and projects, and include expenses for operating as well as capital purposes.

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

	2014	2013
Balance, beginning of year	\$ 66,576,146	\$ 44,202,143
Contributions received during the year:		
Grant from the Province of BC	11,000,000	37,000,000
Investment income	1,841,025	1,911,436
	79,417,171	83,113,579
Amounts recognized as revenue during the period	(15,145,879)	(16,608,640)
Amounts applied toward capital assets purchased during the period	(77,534)	(32,468)
Adjustment to fair value of financial instruments	-	103,675
Balance, end of year	\$ 64,193,758	\$ 66,576,146

(b) Deferred contributions relating to capital assets:

	2014	2013
Balance, beginning of year	\$ 56,332	\$ 97,164
Allocation of deferred contributions	77,534	32,468
Amounts amortized to revenue	(41,244)	(73,300)
Balance, end of year	\$ 92,622	\$ 56,332

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

6. Deferred contributions (continued):

(c) Deferred contributions relating to sponsored projects with restricted funding:

	2014	2013
Balance, beginning of year	\$ 16,066,946	\$ 15,513,227
Amounts received for		
Sponsored projects - Province of British Columbia:		
- Strategy for Patient-Oriented Research	2,000,000	-
- Cerebrospinal Venous Insufficiency	-	500,000
- Alzheimer's Disease Research	-	2,000,000
Sponsored projects - Other Organizations:		
- Healthy Minds, Healthy People	-	1,000,000
- BC Influenza Vaccine Program	-	500,000
- BC Patient Safety & Quality Council	3,330	200,000
- Interior Health	1,500,000	-
	19,570,276	19,713,227
Amounts recognized as revenue	(4,316,557)	(3,646,281)
Balance, end of year	\$ 15,253,719	\$ 16,066,946

The balance of deferred contributions for sponsored projects is comprised of the following:

	2014	2013
BC Patient Safety & Quality Council	\$ 85,905	\$ 200,000
Cerebrospinal Venous Insufficiency	300,000	500,000
BC Influenza Vaccine Program	466,666	500,000
Health Services and Policy Research Support Network	738,312	1,500,028
BC Nursing Research Initiative	890,626	2,805,331
Healthy Minds, Healthy People	1,000,000	1,000,000
Children and Youth with Special Needs	1,339,168	1,339,168
Interior Health	1,500,000	-
Human Papillomavirus 2	1,777,173	1,777,173
Alzheimer's Disease Research	1,996,398	2,000,000
Strategy for Patient Oriented Research	2,000,000	-
Vancouver Island Research Capacity Building	3,159,471	4,445,246
	\$ 15,253,719	\$ 16,066,946

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

7. 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 or strategic projects aimed at fulfilling the Foundation's mandate. Some of the commitments made through these granting programs and projects have terms that span more than one fiscal year. Such grants have on-going eligibility criteria and consequently, grant commitments are expensed in the period that the payment is to be made.

The following table summarizes grant commitments approved by the Foundation, by major grant program or project:

	Grant commitments for the years ending March 31		Total
	2015	2016 and thereafter	
Grant Program or Project:			
Career	\$ 1,455,416	\$ -	\$ 1,455,416
Trainee	1,122,334	5,958	1,128,292
Technology methodology platforms	116,667	-	116,667
Monitoring, evaluation, learning system	221,693	-	221,693
Knowledge translation	137,389	-	137,389
Other	116,667	100,000	216,667
	<u>\$ 3,170,166</u>	<u>\$ 105,958</u>	<u>\$ 3,276,124</u>

(b) Grant commitments - Sponsored projects:

Through a variety of specialized granting programs, the Foundation also may commit significant amounts of project funding to providing peer-reviewed research awards aimed at fulfilling each project's specific mandate. Some of the commitments made through these granting programs have terms that span more than one fiscal year. Such grants have on-going eligibility criteria and consequently, grant commitments are expensed in the period that the payment is to be made.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

7. Commitments (continued):

(b) Grant commitments – Sponsored projects (continued):

The following table summarizes grant commitments approved by the Foundation, by each sponsored project:

	Grant commitments for the years ending March 31		Total
	2015	2016 and thereafter	
Sponsored projects:			
Health Services & Policy Research Support Network:			
- CIHR partnerships	\$ 171,158	\$ 67,334	\$ 238,492
Human Papillomavirus 2			
- Long-term vaccine evaluation	324,167	431,250	755,417
BC Nursing Research Initiative			
- Nursing Health Services Research Network	125,000	-	125,000
- Research Project	62,385	-	62,385
- Commissioned Research	41,647	-	41,647
- Investigative Team	150,000	-	150,000
Vancouver Island Capacity Building			
- Network Grant	114,729	-	114,729
Cerebrospinal Venous Insufficiency	200,000	100,000	300,000
BC Influenza Vaccine Program	16,666	-	16,666
	\$ 1,205,752	\$ 598,584	\$ 1,804,336

(c) Office space and equipment lease commitments:

The Foundation rents office space under a long-term lease that expires October 31, 2016 and provides for an additional five-year extension at the option of the Foundation.

The Foundation also leases various types of office equipment.

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

Years ending March 31:		
2015		\$ 516,273
2016		519,489
2017		280,590
		\$ 1,316,352

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

8. Financial risk management:

The Foundation is exposed to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

(a) Credit risk:

Credit risk is the risk of financial loss to the Foundation if a counterparty to a financial instrument fails to meet its contractual obligations. The Foundation's investments in any term deposits, bonds, income funds and equities are subject to credit risk. The maximum exposure to credit risk on these instruments is their carrying value. The Foundation manages the risk by retaining professional investment counselors who act in accordance with the Foundation's investment policies. These policies include asset mix guidelines and minimum investment grade levels for each asset class.

Other credit risks can arise from holding receivables. The Foundation has minimal accounts receivable, other than from government and as such the credit risk is minimal.

(b) Liquidity risk:

Liquidity risk is the risk that the Foundation will not be able to meet its financial obligations as they fall due. The majority of the Foundation's assets are held as short term investments that can be readily liquidated and therefore the Foundation's liquidity risk is considered minimal. In addition, the Foundation aims to retain a sufficient cash position to manage liquidity.

(c) Market risk:

Market risk is the risk that changes in market prices, as a result of changes in foreign exchange rates, interest rates and equity prices, will affect the Foundation's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while earning an acceptable return.

(i) Currency risk:

Investments in foreign securities are exposed to currency risk due to fluctuations in foreign exchange rates.

The Foundation holds minimal investments in foreign currencies as such the risk is minimal.

MICHAEL SMITH FOUNDATION FOR HEALTH RESEARCH

Notes to Financial Statements (continued)

Year ended March 31, 2014

8. Financial risk management (continued):

(c) Market risk (continued):

(ii) Interest rate risk:

Interest rate risk relates to the risk that changes in interest rates will affect the fair value or future cash flows of financial instruments held by the Foundation. The Foundation is invested in term deposits and income funds that may be impacted by changes in the market interest rate.

The Foundation manages interest rate risk on term deposits by choosing instruments that have fixed rates of return and terms that will match the projected cash flow requirements. Interest rate risk on income funds is managed through professional investment counselors, by holding instruments which have a high liquidity in the marketplace or by choosing instruments with fixed terms that align with projected cash flow requirements.

9. Comparative Information:

Certain comparative information has been reclassified to conform to the financial statement presentation adopted for the current year.