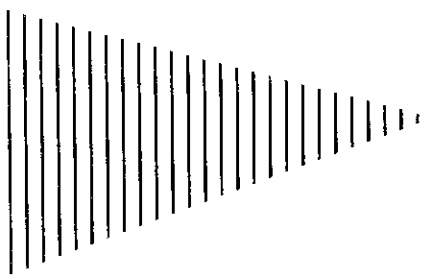


Consolidated financial statements

The Royal Conservatory of Music

August 31, 2016



Building a better
working world

Independent auditors' report

To the Members of
The Royal Conservatory of Music

We have audited the accompanying consolidated financial statements of **The Royal Conservatory of Music**, which comprise the consolidated balance sheet as at August 31, 2016, and the consolidated statements of operations, changes in net assets and cash flows for the year then ended, and 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 the auditors' 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, the auditors 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 audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of **The Royal Conservatory of Music** as at August 31, 2016 and the results of its operations and its cash flows for the year then ended in accordance with Canadian accounting standards for not-for-profit organizations.

Toronto, Canada
November 9, 2016

Ernst & Young LLP

Chartered Professional Accountants
Licensed Public Accountants



The Royal Conservatory of Music

Consolidated balance sheet

[in thousands of dollars]

As at August 31

| | 2016 \$ | 2015 \$ |
|---|----------------|----------------|
| Assets [note 6[d]] | | |
| Current | | |
| Cash | 4,364 | 4,904 |
| Accounts receivable | 4,466 | 3,229 |
| Inventory [note 3] | 1,434 | 1,998 |
| Prepaid expenses | 161 | 190 |
| Total current assets | 10,425 | 10,321 |
| Investments [note 4] | 18,519 | 30,520 |
| Capital assets, net [note 5] | 127,291 | 131,415 |
| | 156,235 | 172,256 |
| Liabilities and net assets | | |
| Current | | |
| Accounts payable and accrued liabilities | 4,017 | 4,797 |
| Accrued interest on long-term indebtedness | 27 | 3,234 |
| Deferred revenue | 3,857 | 3,492 |
| Deferred contributions [note 8] | 8,730 | 8,485 |
| Current portion of long-term indebtedness [note 6[a]] | 545 | — |
| Total current liabilities | 17,176 | 20,008 |
| Accrued benefit liability [note 13[b]] | 1,553 | 1,331 |
| Long-term indebtedness [note 6[a]] | 66,497 | 77,643 |
| Total liabilities | 85,226 | 98,982 |
| Deferred capital asset contributions [note 9] | 49,580 | 51,116 |
| Commitments [note 7] | | |
| Net assets | | |
| Endowments [note 10] | 31,619 | 29,817 |
| Deficit | (10,190) | (7,659) |
| Total net assets | 21,429 | 22,158 |
| | 156,235 | 172,256 |

See accompanying notes

On behalf of the Board:



Director



Director

The Royal Conservatory of Music

Consolidated statement of operations

[in thousands of dollars]

Year ended August 31

| | 2016 | 2015 |
|--|----------------|----------------|
| | \$ | \$ |
| Revenue | | |
| Tuition and examination fees <i>[note 12]</i> | 20,003 | 19,021 |
| Publication sales | 6,027 | 6,587 |
| Other earned revenue <i>[notes 4[c] and 10[b]]</i> | 6,509 | 5,909 |
| Contributions restricted for special purposes <i>[note 8]</i> | 9,646 | 10,146 |
| Other donations and bequests <i>[note 8]</i> | 2,399 | 3,865 |
| | 44,584 | 45,528 |
| Expenses | | |
| Program costs | 31,833 | 31,043 |
| Fundraising and general support | 6,154 | 6,835 |
| Cost of goods sold related to publication sales | 2,024 | 2,760 |
| Scholarships and bursaries <i>[note 12]</i> | 2,141 | 1,919 |
| | 42,152 | 42,557 |
| Excess of revenue over expenses before the following | 2,432 | 2,971 |
| Interest expense <i>[note 6[e]]</i> | (4,104) | (4,066) |
| Amortization of capital assets | (4,361) | (4,427) |
| Amortization of deferred capital asset contributions <i>[note 9]</i> | 1,786 | 2,123 |
| Gain on extinguishment of debt, net <i>[note 6[b]]</i> | 1,827 | — |
| Deficiency of revenue over expenses for the year | (2,420) | (3,399) |

See accompanying notes

The Royal Conservatory of Music

Consolidated statement of changes in net assets

[in thousands of dollars]

Year ended August 31

| | 2016 | | 2015 | |
|--|------------|----------|------------|---------|
| | Endowments | Deficit | Endowments | Deficit |
| | \$ | \$ | \$ | \$ |
| | [note 10] | | [note 10] | |
| | 29,817 | (7,659) | 22,158 | (4,134) |
| | — | (2,420) | (2,420) | (3,399) |
| | 631 | — | 631 | — |
| | 1,171 | — | 1,171 | — |
| | — | — | — | — |
| | — | (111) | (111) | (126) |
| | 31,619 | (10,190) | 21,429 | (7,659) |
| | | | 29,817 | 22,158 |
| | | | | (3,399) |
| | | | | 755 |
| | | | | 2,663 |
| | | | | 2 |
| | | | | (126) |
| | | | | 22,158 |

Net assets, beginning of year

Deficiency of revenue over expenses for the year

Endowment contributions

Income related to endowment net assets in excess of amount available for spending [note 10[b]]

Transfer from deferred contributions [note 10[a]]

Re-measurement related to employee future benefits

Net assets, end of year

See accompanying notes

The Royal Conservatory of Music

Consolidated statement of cash flows

[in thousands of dollars]

Year ended August 31

| | 2016 | 2015 |
|--|----------------|----------------|
| | \$ | \$ |
| Operating activities | | |
| Deficiency of revenue over expenses for the year | (2,420) | (3,399) |
| Add (deduct) items not involving cash | | |
| Amortization of capital assets | 4,355 | 4,427 |
| Amortization of deferred capital asset contributions | (1,786) | (2,123) |
| Penalty, forgiveness and gain on extinguishment of debt | (1,827) | — |
| Increase in accrued benefit liability | 111 | 100 |
| Unrestricted donation held in shares at year end | (71) | — |
| | <u>(1,638)</u> | <u>(995)</u> |
| Net change in non-cash working capital balances related to operations <i>[note 14]</i> | (4,046) | 1,243 |
| Cash (used in) provided by operating activities | <u>(5,684)</u> | <u>248</u> |
| Investing activities | | |
| Purchase of capital assets | (50) | (550) |
| Sale (purchase) of investments, net | 13,373 | (1,217) |
| Cash provided by (used in) investing activities | <u>13,323</u> | <u>(1,767)</u> |
| Financing activities | | |
| Repayment of long-term indebtedness | (8,774) | — |
| Contributions received for capital purposes | 69 | 62 |
| Endowment contributions | 526 | 755 |
| Cash (used in) provided by financing activities | <u>(8,179)</u> | <u>817</u> |
| Net decrease in cash during the year | (540) | (702) |
| Cash, beginning of year | 4,904 | 5,606 |
| Cash, end of year | <u>4,364</u> | <u>4,904</u> |

See accompanying notes

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

1. Description of the organization

The Royal Conservatory of Music [the "RCM"] is an educational institution dedicated to developing human potential through music and arts education.

The RCM was established in 1886. From 1919 to 1991 it operated as a division of the University of Toronto. It was incorporated in its present form in 1991 by *Special Act* of the Legislature of the Province of Ontario. In 1991, the University of Toronto transferred certain assets and liabilities to the RCM and autonomous operations commenced.

The RCM is a registered charitable organization under the *Income Tax Act* (Canada) and, as such, is exempt from income taxes under Registration Number 10793 5413 RR0001.

The RCM operates principally from The TELUS Centre for Performance and Learning [the "TELUS Centre"], located at [REDACTED]. The TELUS Centre includes classrooms and studios, a media centre, library, a multipurpose rehearsal hall and Koerner Hall, an acoustically excellent 1,135 seat concert hall that provides the venue in which the RCM presents performances by accomplished artists to its students and the community.

The RCM's Conservatory School provides programs for children and adults. The Glenn Gould School and the Taylor Performance Academy for Young Artists provide training for students working toward performance and teaching careers. The Learning Through the Arts program provides national and international leadership in integrated arts education. The RCM also develops print music and pedagogical material for teaching and learning and conducts examinations in music nationally and internationally.

In the United States, examinations are conducted by the Music Development Program through The Royal Conservatory of America Corporation ["RCAC"], a New York tax-exempt not-for-profit corporation of which the RCM is the sole member.

The RCM holds the shares of the Frederick Harris Music Co., Limited ["FHMC"] in trust pursuant to an agreement made in December 1944 with the late Frederick Harris. FHMC publishes and sells music publications for music teachers and their students and is the exclusive publisher of all materials designated as publications of the RCM and the Music Development Program. FHMC is incorporated under the laws of Ontario. It is a not-for-profit corporation and, as such, has claimed exemption from income taxes under Section 149(1)(l) of the *Income Tax Act* (Canada). Under Amended Articles of Incorporation, FHMC is not permitted to pay dividends but may distribute funds for charitable, social or civic purposes. The net earnings of FHMC are to be used for the support of musical education.

The RCM has three other related organizations: Royal Conservatory of Music Foundation [in Canada], which is controlled by RCM, and the Royal Conservatory of Music Foundation [in the United States], and the Royal Conservatory of Music Foundation [in the United Kingdom], which are not controlled by RCM. These incorporated, non-taxable organizations raise and hold funds for the benefit of the RCM.

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

2. Significant accounting policies

These consolidated financial statements were prepared in accordance with Part III of the *Chartered Professional Accountants of Canada* ["CPA Canada"] Handbook – Accounting, which sets out generally accepted accounting principles for not-for-profit organizations in Canada and includes the significant accounting policies described hereafter.

Controlled not-for-profit entities

FHMC, the shares of which are held in trust, RCAC and the Royal Conservatory of Music Foundation [in Canada] are controlled organizations and are consolidated into the accounts of RCM.

Financial instruments

Investments reported at fair value consist of investments in pooled funds and any investments in fixed income securities that RCM designates upon purchase to be measured at fair value. Transactions are recorded on a trade-date basis and transaction costs are expensed as incurred.

Investments in fixed income securities not designated to be measured at fair value are initially recorded at fair value plus transaction costs and are subsequently measured at amortized cost using the straight line method, less any provision for impairment.

Other financial instruments, including accounts receivable, accounts payable and long-term indebtedness, are initially recorded at fair value, net of transaction costs, and subsequently measured at amortized cost, less any reduction for impairment.

Inventory

Inventory is recorded at the lower of cost [first-in, first-out basis] and net realizable value.

Capital assets

Capital assets are recorded at cost. For contributed capital assets, cost is considered to be fair value at the date of contribution. The cost of capital assets with limited lives is amortized and recognized as an expense over the useful lives of the assets on a straight-line basis at the following annual rates:

| Tangible | |
|------------------------------------|----------------------------|
| Building and building improvements | 2.5% to 5% |
| Leasehold improvements | Over the term of the lease |
| Furniture, equipment and computers | 20% to 33% |
| Musical instruments | 5% |
| Intangible | |
| Software | 33% |

Assets leased on terms that transfer substantially all of the benefits and risks of ownership to the RCM are accounted for as capital leases, as though the asset had been purchased and a liability incurred. All other leases are accounted for as operating leases.

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

Collections

Collections of antique musical instruments and rarities held by the RCM are not recognized in the consolidated financial statements.

Life insurance policies

The cash surrender value of donated life insurance policies is recorded as an asset and annual increments are recognized in other earned revenue.

Revenue recognition

The RCM follows the deferral method of accounting for contributions, which include donations and government grants. Grants and bequests are recorded when received or receivable if the amount to be received can be reasonably estimated and collection is reasonably assured. Other donations are recorded when received, since pledges are not legally enforceable claims. Unrestricted contributions are recognized as revenue when initially recorded in the accounts. Externally restricted contributions, except endowment contributions, are deferred when initially recorded in the accounts and recognized as revenue in the year in which the related expenses are recognized. Externally restricted endowment contributions are recognized as direct increases in net assets when recorded in the accounts.

Tuition and examination fees are recognized as revenue when courses or examinations are held. Performance and rental revenue is recognized on the date of the performance or event. Publication sales and other revenue is recognized at point of sale or when the service has been provided.

Contributed materials and services

Contributed materials and services are not recognized in these consolidated financial statements.

Foreign currency transactions

Foreign currency transactions and the translation of the results and financial position of RCAC, which has a US dollar functional currency, are translated as follows:

Monetary assets and liabilities are translated into Canadian dollars at the exchange rate in effect at the consolidated balance sheet date, and non-monetary items are translated at the prevailing historical rate at the time of the transaction. Revenue and expenses arising from foreign currency transactions are translated into Canadian dollars at the exchange rate in effect at the transaction date.

Exchange gains and losses are included in the consolidated statement of operations.

Employee future benefits

Contributions to a defined contribution pension plan are expensed in the consolidated statement of operations when due.

The RCM accounts for its obligations under a defined benefit retirement compensation arrangement using the immediate recognition approach. The RCM recognizes the amount of the accrued benefit obligation measured at the consolidated balance sheet date. Current service and finance costs are expensed during the year, while

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

re-measurements and other items, representing actuarial gains and losses and past service costs, are recognized as a direct increase or decrease in the deficit. The accrued benefit obligation is determined based on an actuarial valuation report prepared using accounting assumptions. This report is required to be prepared at least on a triennial basis. During those years where an actuarial valuation is not prepared, RCM estimates the obligation.

Allocation of expenses

The costs of each function include the costs of personnel and other expenses that are directly related to the function. Building costs are attributed based on square footage of use. Information technology costs are attributed based on the functional application of software or number of people employed, as appropriate. General support and other costs are not allocated.

3. Inventory

Inventory consists of the following:

| | 2016 | 2015 |
|----------------------|--------------|--------------|
| | \$ | \$ |
| Prepublication costs | 201 | 137 |
| Finished goods | 1,233 | 1,861 |
| | <u>1,434</u> | <u>1,998</u> |

The cost of inventory recognized in cost of goods sold amounts to \$1,629 [2015 – \$2,255]. Included in this amount is \$172 [2015 – (\$32)] in connection with the change in the inventory obsolescence provision.

4. Investments

[a] Investments, at market value, consist of the following:

| | 2016 | 2015 |
|--|---------------|---------------|
| | \$ | \$ |
| Investments held for endowment net assets <i>[note 4[b]]</i> | 17,076 | 29,851 |
| Donated shares | 201 | — |
| Secured loan <i>[note 4[c]]</i> | 65 | 60 |
| Term deposits | 38 | — |
| Life insurance policy | 1,139 | 609 |
| | <u>18,519</u> | <u>30,520</u> |

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

- [b] The underlying mix of the RCM's investments held for endowments, which include units in pooled funds, is as follows:

| | 2016 | | 2015 | |
|--------------------------|---------------|--------------|---------------|--------------|
| | \$ | % | \$ | % |
| Cash | 1,065 | 6.2 | 1,502 | 5.0 |
| Fixed income alternative | — | — | 5,926 | 19.9 |
| Canadian equities | 3,991 | 23.4 | 4,769 | 16.0 |
| Foreign equities | 12,020 | 70.4 | 17,654 | 59.1 |
| | 17,076 | 100.0 | 29,851 | 100.0 |

The fixed income alternative investments were comprised of units in absolute return funds that seek returns based on changes in interest rates and/or credit spreads in major markets.

- [c] The secured loan receivable is interest free and matures in 2022 with a repayment value of \$100. Interest income of \$5 [2015 – \$4] is included in other earned revenue in the consolidated statement of operations.

5. Capital assets

- [a] Capital assets consist of the following:

| | 2016 | | |
|------------------------------------|----------------|--------------------------|----------------|
| | Cost | Accumulated amortization | Net book value |
| | \$ | \$ | \$ |
| Tangible | | | |
| Land | 17,000 | — | 17,000 |
| Building and building improvements | 139,384 | 31,623 | 107,761 |
| Furniture, equipment and computers | 3,568 | 3,297 | 271 |
| Musical instruments [note 5[b]] | 4,260 | 2,287 | 1,973 |
| Intangible | | | |
| Software | 4,251 | 3,965 | 286 |
| | 168,463 | 41,172 | 127,291 |

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

| | 2015 | | |
|--|----------------|-----------------------------|-------------------|
| | Cost | Accumulated amortization | Net book value |
| | \$ | \$ | \$ |
| Tangible | | | |
| Land | 17,000 | — | 17,000 |
| Building and building improvements | 139,382 | 27,972 | 111,410 |
| Furniture, equipment and computers | 3,503 | 3,180 | 323 |
| Musical instruments <i>[note 5[b]]</i> | 4,102 | 2,124 | 1,978 |
| Intangible | | | |
| Software | 4,251 | 3,547 | 704 |
| | <u>168,238</u> | <u>36,823</u> | <u>131,415</u> |

As at August 31, 2016, the cost of software includes nil [2015 - \$511] that is under development and not being amortized.

In 2015, RCM wrote-off 1,173 of fully amortized capital assets.

- [b] Contributed capital assets with a fair value of \$181 [2015 - \$327] have been recorded as tangible capital assets offset by an equal increase in deferred capital asset contributions *[note 9]*.

6. Bank and other indebtedness

- [a] Bank and other indebtedness consists of the following:

| | 2016 | | |
|---|------------|---------------|---------------|
| | Current | Long-term | Total |
| | \$ | \$ | \$ |
| Debenture 003, due February 26, 2048 <i>[note 6[b]]</i> | 545 | 66,497 | 67,042 |
| | <u>545</u> | <u>66,497</u> | <u>67,042</u> |
| | | | |
| | 2015 | | |
| | Current | Long-term | Total |
| | \$ | \$ | \$ |
| Debenture 002, due May 3, 2030 <i>[note 6[b]]</i> | — | 77,643 | 77,643 |
| | <u>—</u> | <u>77,643</u> | <u>77,643</u> |

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

- [b] Effective August 26, 2016, the RCM and Ontario Infrastructure and Lands Corporation ["Infrastructure Ontario"] entered into an Amended and Restated Financing Agreement [the "Agreement"] pursuant to which the RCM extinguished Debenture 002 and issued Debenture 003.

Debenture 003, which is collateralized by a mortgage on the TELUS Centre, matures on February 26, 2048. The RCM is entitled to prepay all or part of the debenture at any time, subject to certain penalties. Beginning November 26, 2016, the RCM will make equal quarterly blended payments of principal and interest in each loan year which aggregate to a specified annual amount. The specified annual amount begins at \$2,500 in the first year and increases at a compound rate of 2% in each subsequent year through November 26, 2047. As at August 26, 2016, the Infrastructure Ontario indicative interest rate was 2.925%; as a result, on the date of issue, the fair value of Debenture 003 was \$67,042.

In addition to the principal of \$77,643, accrued interest of \$7,281 was payable immediately prior to the extinguishment of Debenture 002. The RCM was also liable for a penalty of \$15,041 on prepayment, resulting in a total consideration payable on extinguishing Debenture 002 of \$99,965. Under the terms of the Agreement, IO extended forgiveness of \$15,000 and the RCM made a payment in cash of \$16,096. As a result, a gain of \$1,827 was realized on the extinguishment of Debenture 002.

Minimum payments due in the next five years under Debenture 003 are: 2017 – \$2,500; 2018 – \$2,550; 2019 – \$2,601; 2020 – \$2,653; and 2021 – \$2,706

- [c] ██████████ has provided the RCM with a \$5,000 revolving credit facility for general operating purposes. Interest on loans and overdrafts is charged at ██████████ prime rate plus 1% [August 31, 2015 – 1%]. Drawings against this facility are due on demand. As at August 31, 2016, ██████████ had issued a letter of guarantee in the amount of \$2,198 [2015 – \$1,274] and subsequent to year end was increased to \$2,308.
- [d] Substantially all of the RCM's assets are pledged as collateral against indebtedness to ██████████ and Infrastructure Ontario.
- [e] Interest expense of \$4,104 [2015 – \$4,066] was recorded with respect to debt incurred in the year.

7. Operating leases

The RCM's future minimum annual lease payments under operating leases in respect of equipment are: 2017 – \$139; 2018 – \$86; 2019 – \$86 and 2020 – \$14.

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

8. Deferred contributions

[a] Deferred contributions represent unspent externally restricted donations and government grants. The changes in the deferred contributions balance are as follows:

| | 2016 \$ | 2015 \$ |
|--|-----------------|------------|
| Balance, beginning of year | 8,485 | 9,010 |
| Government grants | 2,998 | 2,272 |
| Donations received for annual scholarships and bursaries | 1,470 | 1,470 |
| Amount made available for spending related to endowment net assets [notes 10[b] and 11] | 1,197 | 1,031 |
| Other restricted donations | 5,026 | 4,674 |
| Transfer to endowment net assets [note 10[a]] | | (2) |
| Amount recognized as revenue during the year | (10,446) | (9,970) |
| Balance, end of year | 8,730 | 8,485 |

[b] The deferred contributions balance consists of unspent amounts restricted for the following purposes:

| | 2016 \$ | 2015 \$ |
|----------------------------|--------------|------------|
| Programs | 6,383 | 6,037 |
| Scholarships and bursaries | 2,347 | 2,448 |
| | 8,730 | 8,485 |

9. Deferred capital asset contributions

Deferred capital asset contributions represent the unamortized amount of donations and grants received for the purchase of capital assets. The amortization of deferred capital asset contributions is recorded in the consolidated statement of operations. The changes in the deferred capital asset contributions balance are as follows:

| | 2016 \$ | 2015 \$ |
|---|----------------|------------|
| Balance, beginning of year | 51,116 | 52,850 |
| Add contributions received for capital purposes [note 5[b]] | 250 | 389 |
| Less amortization of deferred capital asset contributions | (1,786) | (2,123) |
| Balance, end of year | 49,580 | 51,116 |

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

10. Endowments

- [a] Endowments included in these consolidated financial statements exclude those with the Ontario Arts Foundation ["OAF"] [note 11] and consist of amounts where the amount made available for spending is restricted primarily for scholarships and bursaries.

During the year ended August 31, 2015, \$2 was transferred to endowment net assets at the direction of the donor.

- [b] The endowment net assets consist of amounts subject to donor restrictions relating to maintaining the principal and using the income in accordance with the various purposes established by the donor or the Board.

The Board has adopted a policy with the objective of protecting the real value of the endowment net assets by limiting the amount of income made available for spending and requiring the reinvestment of any income earned in excess of this limit. The amount available for spending is to be calculated based on 3% of the market value of individual funds at December 31 of the prior year unless a different basis of distribution has been stipulated by the donor. The preservation of capital is recorded as a direct increase in endowment net assets. In any year, should net investment income not be sufficient to fund the amount required for spending, an amount may be transferred from endowment net assets to deferred contributions for this purpose.

In fiscal 2016, income of \$2,329 [2015 – \$3,666] was earned on endowment net assets. An amount of \$1,158 [2015 – \$1,003] was made available for spending. Of the amount made available for spending, \$79 [2015 – \$79] was unrestricted and recorded in other revenue and \$1,079 [2015 – \$924] was restricted and recorded in deferred contributions [note 8]. The difference of \$1,171 [2015 – \$2,663], representing preservation of capital, was added directly to endowment net assets.

11. Endowments with the Ontario Arts Foundation

In 1999, the Province of Ontario established the Arts Endowment Program with the OAF. Under this program, money raised by eligible arts organizations, specifically for endowment purposes, was matched. For each participating arts organization, a separate trust fund was established and is maintained by the OAF. From time to time, at the discretion of the OAF, these organizations receive income from the funds held for their benefit. During the year ended August 31, 2016, the RCM received \$118 [2015 – \$107] from the OAF. These contributions are used by the RCM to award scholarships under conditions consistent with the terms of the endowments held by the OAF.

As at August 31, 2016, the OAF is holding capital amounting to \$1,908 [2015 – \$1,908] and undistributed income of \$723 [2015 – \$635] for the benefit of the RCM. These funds are held in trust by the OAF and are not recorded in these consolidated financial statements.

12. Tuition fees

Tuition fees include an amount equal to scholarships and bursaries awarded to students of \$2,141 [2015 – \$1,919]. Substantially all these scholarships and bursaries are funded by contributions restricted for special purposes recognized during the year in the consolidated statement of operations.

The Royal Conservatory of Music

Notes to consolidated financial statements

[all amounts in thousands of dollars, except where noted]

August 31, 2016

13. Employee future benefits

- [a] The faculty defined contribution pension plan was formally wound up in 2015 and the funds distributed to the pension plan members. This benefit has been converted to a group RRSP.
- [b] The RCM has established a defined benefit retirement compensation arrangement for the benefit of the Chief Executive Officer. Based on an actuarial valuation report prepared as of August 31, 2016, the accrued benefit liability as at August 31, 2016 was \$1,553 [2015 – \$1,331].

14. Consolidated statement of cash flows

The net change in non-cash working capital balances is comprised of the following:

| | 2016 | 2015 |
|--|----------------|--------------|
| | \$ | \$ |
| Decrease (increase) in accounts receivable | (1,237) | 481 |
| Decrease in inventory | 564 | 206 |
| Decrease in prepaid expenses | 29 | 52 |
| Decrease in accounts payable and accrued liabilities | (780) | (35) |
| Increase (decrease) in accrued interest | (3,207) | 440 |
| Increase in deferred revenue | 365 | 622 |
| Increase in deferred contributions | 220 | (523) |
| | <u>(4,046)</u> | <u>1,243</u> |

As at August 31, 2016, deferred contributions include \$25 related to donated shares.

15. Financial instruments

The RCM is exposed to various risks with respect to financial instruments.

Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The RCM's main credit risk relates to its accounts receivable. Accounts receivable are recorded net of an allowance for doubtful accounts of \$24 [2015 – \$144].

Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The RCM's currency risk arises from international equities that are held within the pooled fund in which the RCM holds units and cash, and accounts receivable and accounts payable balances related to RCAC.

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[all amounts in thousands of dollars, except where noted]

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Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The RCM is exposed to interest rate price risk with respect to its fixed rate debt and its investment in pooled funds which holds bonds and other debt instruments, the values of which will fluctuate with changes in market interest rates. In addition, the RCM is exposed to interest rate cash flow risk since the interest rate on the RCM's operating line of credit with RBC is linked to the bank's prime rate which changes from time to time.

Liquidity risk

Liquidity risk is the risk that the RCM will encounter difficulty in meeting obligations associated with financial liabilities. The RCM is exposed to this risk in respect of its accounts payable and accrued liabilities and its various other debt obligations.

Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices [other than those arising from interest rate risk or currency risk], whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. The RCM is exposed to other price risk with respect to its investment in pooled funds.