



*Consolidated
Departmental
Financial
Statements*

2013–2014
(UNAUDITED)



STATEMENT OF MANAGEMENT RESPONSIBILITY INCLUDING INTERNAL CONTROL OVER FINANCIAL REPORTING (UNAUDITED)

Responsibility for the integrity and objectivity of the accompanying financial statements for the year ended March 31, 2014, and all information contained in these statements rests with the management of Department of National Defence (DND). These financial statements have been prepared by management using Government's accounting policies, which are based on Canadian public sector accounting standards.

Management is responsible for the integrity and objectivity of the information in these financial statements. Some of the information in the financial statements is based on management's best estimates and judgment, and gives due consideration to materiality. To fulfill its accounting and reporting responsibilities, management maintains a set of accounts that provides a centralized record of the DND's financial transactions. Financial information submitted in the preparation of the *Public Accounts of Canada*, and included in the DND's *Departmental Performance Report*, is consistent with these financial statements.

Management is also responsible for maintaining an effective system of Internal Control over Financial Reporting (ICFR) designed to provide reasonable assurance that financial information is reliable, that assets are safeguarded and that transactions are properly authorized and recorded in accordance with the *Financial Administration Act* and other applicable legislation, regulations, authorities and policies.

Management seeks to ensure the objectivity and integrity of data in its financial statements through careful selection, training, and development of qualified staff; through organizational arrangements that provide appropriate divisions of responsibility; through communication programs aimed at ensuring that regulations, policies, standards, and managerial authorities are understood throughout DND; and through conducting an annual assessment of the effectiveness of ICFR.

The system of ICFR is designed to mitigate risks to a reasonable level based on an on-going process to identify, assess effectiveness and adjust as required key risks and associated key controls.

A risk-based assessment of the system of ICFR for the year ended March 31, 2014 was completed in accordance with the Treasury Board *Policy on Internal Control* and the results and action plans are summarized in the annex.

The effectiveness and adequacy of the DND's system of internal control is reviewed by the work of internal audit staff, who conduct periodic audits of the different areas of the DND's operations, and by the DND's Audit Committee, which oversees management's responsibilities for maintaining adequate control systems and the quality of financial reporting.

The financial statements of DND have not been audited.

// Signed by //

Richard B. Fadden

Deputy Minister
Ottawa, Canada

Date: August 26, 2014

// Signed by //

J.K. Lindsey, CPA, CMA, ICD.D

Chief Financial Officer



CONSOLIDATED STATEMENT OF FINANCIAL POSITION (UNAUDITED)

As at March 31

| (in thousands of dollars) | 2014 | 2013 (Restated note 20) |
|--|-------------------|----------------------------|
| Liabilities | | |
| Accounts payable and accrued liabilities (note 4) | 2,272,421 | 2,910,981 |
| Vacation pay and compensatory leave | 192,682 | 208,959 |
| Deposits and trust accounts (note 5) | 3,345 | 4,167 |
| Deferred revenue (note 6) | 13,780 | 17,617 |
| Canadian Forces pension and insurance accounts (note 7) | 47,102,778 | 47,167,979 |
| Lease obligations for tangible capital assets (note 8) | 425,006 | 480,389 |
| Employee future benefits (note 9) | 1,008,732 | 1,773,358 |
| Remediation liabilities (note 15) | 462,424 | 407,149 |
| Future asset restoration liabilities (note 15) | 1,989 | 3,044 |
| Total liabilities | 51,483,157 | 52,973,643 |
| Financial assets | | |
| Due from Consolidated Revenue Fund | 48,821,701 | 49,584,038 |
| Accounts receivables (note 10) | 888,821 | 189,632 |
| Loans and advances (note 11) | 40,875 | 34,793 |
| Total gross financial assets | 49,751,397 | 49,808,463 |
| Financial assets held on behalf of Government | | |
| Accounts receivables (note 10) | (2,703) | (2,080) |
| Total financial assets held on behalf of Government | (2,703) | (2,080) |
| Total net financial assets | 49,748,694 | 49,806,383 |
| Departmental net debt | 1,734,463 | 3,167,260 |
| Non-financial assets | | |
| Prepaid expenses (note 12) | 623,841 | 610,022 |
| Inventories (note 13) | 6,429,769 | 6,358,695 |
| Tangible capital assets (note 14) | 32,242,722 | 31,754,581 |
| Total non-financial assets | 39,296,332 | 38,723,298 |
| Departmental net financial position | 37,561,869 | 35,556,038 |

Contingent liabilities (note 15)
Contractual obligations (note 16)

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

// Signed by //

Richard B. Fadden
Deputy Minister
Ottawa, Canada

Date: August 26, 2014

// Signed by //

J.K. Lindsey, CPA, CMA, ICD.D
Chief Financial Officer



CONSOLIDATED STATEMENT OF OPERATIONS AND DEPARTMENTAL NET FINANCIAL POSITION (UNAUDITED)

For the year ended March 31

| (in thousands of dollars) | 2014 Planned Results (Restated) | 2014 | 2013 (Restated note 20) |
|--|---------------------------------------|--------------------|----------------------------|
| Expenses | | | |
| Defence Science and Technology | 366,660 | 386,942 | 372,588 |
| Recruiting of Personnel and Initial Training | 1,084,306 | 1,138,213 | 1,235,230 |
| Equipment Acquisition and Disposal | 2,362,025 | 2,144,789 | 2,841,934 |
| Real Property Infrastructure Acquisition and Disposal | 391,063 | 368,962 | 374,098 |
| Maritime Readiness | 2,041,312 | 2,371,497 | 2,410,601 |
| Land Readiness | 3,538,826 | 3,377,420 | 3,976,930 |
| Aerospace Readiness | 1,724,694 | 1,962,823 | 1,916,338 |
| Joint and Common Readiness | 2,314,571 | 1,913,781 | 1,891,966 |
| Situational Awareness | 478,261 | 372,855 | 413,746 |
| Canadian Peace, Stability and Security | 291,913 | 358,170 | 350,717 |
| Continental Peace, Stability and Security | 186,239 | 217,676 | 239,707 |
| International Peace, Stability and Security | 1,583,217 | 1,253,138 | 1,417,435 |
| Defence Team Personnel Support | 1,012,973 | 1,131,811 | 1,791,318 |
| Canadian Identity | 350,010 | 350,727 | 372,983 |
| Environment Protection and Stewardship | 122,820 | 152,827 | 96,105 |
| Non-Security Support | 12,180 | 642 | 3,519 |
| Internal Services | 1,230,189 | 871,148 | 1,298,754 |
| Total expenses | 19,091,259 | 18,373,421 | 21,003,969 |
| Revenues | | | |
| Sale of goods and services | 420,865 | 424,406 | 416,618 |
| Gains on disposals of assets | 35,247 | 22,232 | 36,070 |
| Other | 15,696 | 24,315 | 22,171 |
| Interest and gains on foreign exchange | 8,955 | 8,683 | 11,657 |
| Revenues earned on behalf of Government | (18,263) | (16,336) | (15,842) |
| Total revenues | 462,500 | 463,300 | 470,674 |
| Net cost from continuing operations | 18,628,759 | 17,910,121 | 20,533,295 |
| Transferred operations (note 18) | | | |
| Expenses | 18,428 | 0 | 17,704 |
| Net cost of transferred operations | 18,428 | 0 | 17,704 |
| Net cost of operations before government funding and transfers | 18,647,187 | 17,910,121 | 20,550,999 |
| Government funding and transfers | | | |
| Net cash provided by Government | 18,163,902 | 19,945,461 | 19,594,643 |
| Change in due from Consolidated Revenue Fund | 867,483 | (762,337) | 275,988 |
| Services provided without charge by other government departments (note 17) | 895,448 | 733,909 | 861,165 |
| Transfer of assets and liabilities from (to) other government departments | 0 | (1,081) | (15) |
| Net cost of operations after government funding and transfers | (1,279,646) | (2,005,831) | (180,782) |
| Departmental net financial position — beginning of year | 37,108,052 | 35,556,038 | 35,375,256 |
| Departmental net financial position — end of year | 38,387,698 | 37,561,869 | 35,556,038 |

Segmented information (note 19)

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



CONSOLIDATED STATEMENT OF CHANGE IN DEPARTMENTAL NET DEBT (UNAUDITED)

For the year ended March 31

| (in thousands of dollars) | 2014 Planned Results | 2014 | 2013 (Restated note 20) |
|--|-------------------------|--------------------|----------------------------|
| Net cost of operations after government funding and transfers | (1,279,646) | (2,005,831) | (180,782) |
| Change due to tangible capital assets | | | |
| Acquisition of tangible capital assets | 4,050,075 | 3,012,027 | 3,008,019 |
| Amortization of tangible capital assets | (2,929,019) | (2,377,753) | (2,722,392) |
| Proceeds from disposal of tangible capital assets | (18,145) | (22,431) | (38,672) |
| Loss on disposals of tangible capital assets | (465,423) | (128,995) | (541,366) |
| Adjustments of tangible capital assets | (353,134) | 6,374 | (15,830) |
| Transfer to other government departments | 0 | (1,081) | (15) |
| Total change due to tangible capital assets | 284,354 | 488,141 | (310,256) |
| Change due to inventories | 181,928 | 71,074 | 139,891 |
| Change due to prepaid expenses | 18,165 | 13,819 | (179,073) |
| Net decrease in departmental net debt | (795,199) | (1,432,797) | (530,220) |
| Departmental net debt — beginning of year | 2,683,920 | 3,167,260 | 3,697,480 |
| Departmental net debt — end of year | 1,888,721 | 1,734,463 | 3,167,260 |

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



CONSOLIDATED STATEMENT OF CASH FLOW (UNAUDITED)

For the year ended March 31

| (in thousands of dollars) | 2014 | 2013 (Restated note 20) |
|--|--------------------|----------------------------|
| Operating activities | | |
| Net cost of operations before Government funding and transfers | 17,910,121 | 20,550,999 |
| Non-cash items included in net cost of operations | | |
| Amortization of tangible capital assets | (2,377,753) | (2,722,392) |
| Loss on disposals of tangible capital assets | (128,995) | (541,366) |
| Adjustments of tangible capital assets | 6,374 | (15,830) |
| Services provided without charge by other government departments (note 17) | (733,909) | (861,165) |
| Variations in Statement of Financial Position | | |
| Increase (decrease) in accounts receivables | 698,566 | 31,395 |
| Increase (decrease) in loans and advances | 6,082 | 577 |
| Increase (decrease) in prepaid expenses | 13,819 | (179,073) |
| Increase (decrease) in inventories | 71,074 | 139,891 |
| Decrease (increase) accounts payable and accrued liabilities | 638,560 | 305,905 |
| Decrease (increase) vacation pay and compensatory leave | 16,277 | (4,484) |
| Decrease (increase) deposits and trust accounts | 822 | (301) |
| Decrease (increase) deferred revenue | 3,837 | 5,341 |
| Decrease (increase) Canadian Forces pension and insurance accounts | 65,201 | (110,736) |
| Decrease (increase) employee future benefits | 764,626 | (44,199) |
| Decrease (increase) remediation liabilities | (55,275) | 17,905 |
| Decrease (increase) future asset restoration liabilities | 1,055 | 713 |
| Cash used by operating activities | 16,900,482 | 16,573,180 |
| Capital investing activities | | |
| Acquisitions of tangible capital assets (note 14) | 3,012,027 | 3,008,019 |
| Proceeds on disposal of surplus assets | (22,431) | (38,672) |
| Cash used by capital investing activities | 2,989,596 | 2,969,347 |
| Financing activities | | |
| Payments against / adjustments to capital lease obligations | 55,383 | 52,116 |
| Cash used by financing activities | 55,383 | 52,116 |
| Net cash provided by Government of Canada | 19,945,461 | 19,594,643 |

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



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

1. Authority and Objectives

AUTHORITIES

The Department of National Defence (DND) was established by the *National Defence Act* (NDA). Under section 3 of the NDA, the Minister of National Defence presides over the Department. Under section 4 of the NDA, the Minister has the management and direction of the Canadian Forces (CF) and of all matters relating to national defence. The Minister is also responsible for the construction and maintenance of all defence establishments and works for the defence of Canada, as well as research relating to the defence of Canada and to the development of and improvements in materiel.

OBJECTIVES

On behalf of the people of Canada, the Canadian Armed Forces (CAF) and the Department of National Defence (DND) stand ready to perform three key roles:

- Defend Canada — by delivering excellence at home;
- Defend North America — by being a strong and reliable partner with the United States in the defence of the continent; and
- Contribute to International Peace and Security — by projecting leadership abroad.

These objectives are delivered through the Program Alignment Architecture (PAA) and the following seventeen Programs:

(a) Defence Science and Technology (S&T):

This program provides the Government of Canada with critical scientific knowledge and innovation to address defence and security challenges and needs. The S&T Program includes direction setting, program planning, program management, and capability management, execution and assessment. The program comprises

multi-year projects with activities in research, technology development, analysis and experimentation applied to inform, enable and respond to Canada's defence and security priorities over multiple time horizons extending up to a 20-year outlook. The scientific knowledge and innovation generated from these activities informs decisions on defence capability acquisitions, readiness preparation and the conduct of operations in response to Government priorities. Activities under this program draw on internal capability and make extensive use of partnerships with Canadian industry and academia as well as international organizations.

(b) Recruiting of Personnel and Initial Training:

This program will promote National Defence as a preferred workplace with the general public and to recruit new hires for a broad range of trades and other general, professional and scientific occupations. This involves deepening Defence's connections to the various educational and ethnic communities to attract the right number and mix of people who have the skills needed to contribute in meeting the Defence Mission. Engaging in effective leadership, strategic planning, and targeted outreach activities will ensure proactive measures are taken to address the challenges arising from current labour market pressures for specific skill sets within certain geographic locations. The program will attract, select and enrol personnel and conduct initial training (basic recruit and occupational training) to military members to the Operational Functional Point. This ensures that sufficient personnel are recruited and trained with the needed skills in the appropriate occupation, now and into the future, to meet Defence requirements. This is accomplished through the provision of recruitment centres, recruitment campaigns, advertising and other outreach activities as well as the necessary training staff, facilities and associated supports.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

(c) Equipment Acquisition and Disposal:

This program acquires equipment required for Canadian Armed Forces operations. This includes the acquisition of new and replacement capabilities or capital improvements to in-service equipment and disposes of them at the end of their service life. Equipment Acquisition occurs primarily through collaboration with Public Works and Government Services (PWGSC), Industry Canada (IC) and the vendors. Equipment Acquisition activities include defining requirements, engineering design, sourcing, validation of requirements, developing procurement strategy, contracting, contract negotiation and award, contract administration and management and project management of equipment acquisitions.

(d) Real Property Infrastructure Acquisition and Disposal:

An extensive portfolio of land, works, and buildings and informatics is required to support the delivery of defence operations. The Real Property Infrastructure Acquisition Disposal program aims to ensure that the right real property and informatics is acquired and disposed of, and is available where and when needed, while providing value for money, advancing objectives for the greening of government land and buildings, and adhering to best practices for asset life-cycle management. Program activities include working with stakeholders to define requirements; updating the real property development and management plans; managing projects for new and replacement construction; and identifying and eliminating excess facilities. Real property is acquired through construction and recapitalization, purchase or capital leases, and disposed of through deconstruction, sale or transfer. The activity includes the Capital Assistance Program (CAP) which is a capital contribution program under which National Defence makes financial contributions to support the transfer of infrastructure facilities to provinces, territories, municipalities and/or their agencies. CAP projects support real property goals and objectives by encouraging cost-effective solutions for the provision of infrastructure on bases and wings across Canada.

(e) Maritime Readiness:

This program provides Canada with a combat-capable, multi-purpose Navy. The program will generate and sustain relevant, responsive, combat capable maritime forces that are able to respond to a spectrum of tasks, as may be directed by the Government, within the required response time. This is accomplished by bringing maritime forces to a state of readiness for operations, by assembling, and organizing maritime personnel, supplies, and materiel. This includes the training and equipping of forces and the provision of their means of deployment, sustainment and recovery to defend Canadian interests domestically, continentally and internationally.

(f) Land Readiness:

This program provides Canada with a combat-capable, multi-purpose Army. The program will generate and sustain relevant, responsive, combat capable land forces that are effective across the spectrum of conflict, from peacekeeping and nation building to war fighting. This is accomplished by bringing land forces to a state of readiness for operations, assembling and organizing Land personnel, supplies, and materiel as well as the provision of individual and collective training to prepare land forces to defend Canadian interests domestically, continentally and internationally.

(g) Aerospace Readiness:

This program will provide Canada with a combat-capable, multi-purpose Air Force. The program will generate and sustain relevant, responsive, combat capable aerospace forces that are able to respond to the spectrum of tasks, as may be directed by the Government, within the required response time. This is accomplished by bringing aerospace forces to a state of readiness for operations, by assembling, and organizing aerospace personnel, supplies, and materiel. This includes the training and equipping of aerospace forces and the provision of their means of deployment, sustainment and recovery to defend Canadian interests domestically, continentally and internationally.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

(h) Joint and Common Readiness:

This program will ensure Defence is ready to operate in a joint capacity, as directed by Government, to respond to domestic, continental and international requirements within the required response time. The program will generate and sustain forces for activities, operations and organizations in which elements of at least two services (e.g. Royal Canadian Navy, Canadian Army, Royal Canadian Air Force) participate. This is accomplished through the provision of training of a joint and common nature, the equipping of forces and the provision of their means to deploy in a joint capacity.

(i) Situational Awareness:

The Government of Canada and Defence require an accurate and timely security picture and comprehensive situational awareness and threat knowledge for Canada and abroad. This program provides credible, reliable and sustained intelligence services to Defence in support of decision making and military operations, as well as, support to other government departments in the defence and security of Canada. Work activities include geospatial intelligence, imagery intelligence, signals intelligence, and counter intelligence.

(j) Canadian Peace, Stability and Security:

This program employs the Canadian Armed Forces (CAF) in the conduct of operations to ensure the safety and security of Canadians and the defence of Canada. These operations include protecting Canada's sovereignty, responding to domestic disasters or humanitarian crisis, supporting domestic security requirements, and conducting search and rescue activities. This is accomplished through the mobilization and deployment of forces within Canada. Canada Command* is responsible for the conduct of all CAF domestic operations — routine and contingency — and is the national operational authority for the defence of Canada.

* Canada Command (CanCOM) was dissolved and formally replaced by Canadian Joint Operations Command (CJOC) on October 5, 2012.

(k) Continental Peace, Stability and Security:

This program employs the Canadian Armed Forces in the conduct of operations, both independently and in conjunction with allies, for the defence of North America and its approaches. Activities under this program include continental operations, as required in accordance with Government of Canada policy. This is accomplished through the mobilization and deployment of forces for the defence of North America and its approaches. Canada Command* is responsible for the conduct of all continental operations — routine and contingency — and is the national operational authority for the defence of North America and its approaches.

(l) International Peace, Stability and Security:

This program will contribute to global peace and security by conducting global Canadian Armed Forces (CAF) operations, across the spectrum from humanitarian assistance to combat, in concert with national and international partners, to achieve timely and decisive results in support of Canada's national interests. This is accomplished through the mobilization and deployment of forces internationally. Canadian Expeditionary Force Command** is the operational command responsible for all CAF international operations, with the exception of operations conducted solely by Special Operations Forces elements.

(m) Defence Team Personnel Support:

The Defence Team Personnel Support program will provide a broad spectrum of support services such as financial support for education and housing and facilities services, as well as, benefits to military personnel and their families. This program will also provide learning support to Defence civilians. This program is necessary as the provision of fair and equitable support is a key element of the Social Contract between the nation and its military personnel that is essential to enhance personnel readiness and deployability, and establish the Canadian Armed Forces as an employer of choice and learning institution.

** Canadian Expeditionary Forces Command (CEFCOM) was dissolved and formally replaced by Canadian Joint Operations Command (CJOC) on October 5, 2012.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

(n) Canadian Identity:

This program preserves and promotes Canadian identity by providing youth programs, ceremonial activities and the preservation of military history. The program is necessary to demonstrate the military heritage and proficiency of the Canadian Armed Forces (CAF) to Canadians and inform them of the military profession and practice in Canada. This is realized through initiatives such as ceremonial and band performances, CAF museums, CAF history and heritage books, web content and the Cadets.

(o) Environmental Protection and Stewardship:

This program promotes public health and safety and supports sustainable development on Defence lands and wherever Defence operates. It delivers multi-faceted real property/infrastructure environmental protection and stewardship compliant with applicable legislation and federal policy that extends through every level of departmental decision-making.

(p) Non-Security Support:

Defence is strongly committed to contributing to Canadian society in non-operational roles. The program provides support to develop national competency in defence issues and to the whole of government approach by sharing information with other government departments and non-governmental organizations. This may include the provision of grants to researchers to generate knowledge related to defence issues or provide meteorological or mapping information to other government departments in the interest of information sharing on horizontal initiatives.

(q) Internal Services:

Internal Services are groups of related activities and resources that are administered to support the needs of programs and other corporate obligations of an organization. These groups are: Management and Oversight Services; Communications Services; Legal Services; Human Resources Management Services; Financial Management Services; Information Management Services; Information Technology Services; Real Property Services; Materiel Services; Acquisition Services; and Travel and Other Administrative Services. Internal Services include only those activities and resources that apply across an organization and not to those provided specifically to a program.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

2. Summary of significant accounting policies

These financial statements have been prepared using the Government's accounting policies stated below, which are based on Canadian public sector accounting standards. The presentation and results using the stated accounting policies do not result in any significant differences from Canadian public sector accounting standards.

Significant accounting policies are as follows:

(a) Parliamentary Authorities

The Department is financed by the Government of Canada through Parliamentary authorities. Financial reporting of authorities provided to the Department do not parallel financial reporting according to generally accepted accounting principles since authorities are primarily based on cash flow requirements. Consequently, items recognized in the Consolidated Statement of Operations and Departmental Net Financial Position and the Consolidated Statement of Financial Position are not necessarily the same as those provided through authorities from Parliament. Note 3 provide reconciliation between the bases of reporting. The planned results amounts in the Consolidated Statement of Operations and Departmental Net Financial Position and Consolidated Statement of Change in Departmental Net Debt are the amounts reported in the future-oriented financial statements included in the *2013-14 Report on Plans and Priorities*. The future-oriented financial statements have been reclassified to conform to the current year presentation.

(b) Consolidation

These consolidated financial statements include the accounts of the sub-entities that the deputy head (DH) is accountable for. The accounts of these sub-entities have been consolidated with those of the Department and all inter-organizational balances and transactions have been eliminated. The Department is comprised of DND, the CAF and several related organizations and agencies in the Defence Portfolio, which carry out the Defence mission and are part of the Defence Services Program.

Organizations and agencies that are part of these consolidated financial statements include the following:

- Canadian Cadet Program and the Junior Canadian Rangers;
- Canadian Forces Housing Agency;
- Defence Research and Development Canada;
- Office of the Ombudsman for the Department of National Defence and Canadian Forces;
- Office of the Judge Advocate General; and
- National Search and Rescue Secretariat.

The Military Grievances External Review Committee, the Military Police Complaints Commission, Communications Security Establishment Canada and the Office of the Communications Security Establishment Commissioner are excluded from the consolidation because these organizations are not part of the Defence Services Program, although they fall under the responsibility of the Minister of National Defence.

(c) Net Cash Provided by Government

The Department operates within the Consolidated Revenue Fund (CRF), which is administered by the Receiver General for Canada. All cash received by the department is deposited to the CRF and all cash disbursements made by the Department are paid from the CRF. The net cash provided by the Government is the difference between all cash receipts and cash disbursements including transactions between departments of the Government.

(d) Amounts Due From/To the Consolidated Revenue Fund

Amounts due from or to the CRF are the result of timing differences at year-end between when a transaction affects authorities and when it is processed through the CRF. Amounts due from the CRF represent the net amount of cash that the Department is entitled to draw from the CRF without further authorities to discharge its liabilities.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

(e) Revenues

- Revenues from regulatory fees are recognized in the accounts based on the services provided in the year.
- Funds received in advance from external parties for the provision of goods, services or the use of assets are recorded upon receipt as deferred revenue. These funds are recognized as revenues in the period in which the related expenses are incurred.
- Other revenues are accounted for in the period in which the underlying transaction or event that gave rise to the revenue takes place.

Revenues that are non-respondable are not available to discharge the Department's liabilities. While the DH is expected to maintain accounting control, he has no authority regarding the disposition of non-respondable revenues. As a result, non-respondable revenues are considered to be earned on behalf of the Government of Canada and are therefore presented in reduction of the entity's gross revenues.

(f) Expenses

Expenses are recorded on an accrual basis:

- Transfer payments are recorded as expenses when authorization for the payment exists and the recipient has met the eligibility (or the entitlements) criteria (for grants) or the performance conditions (for contributions) established for the transfer payment program. In situations where grant payments do not form part of an existing program, payments are recorded as expenses when the Government announces a decision to make a non-recurring transfer, provided the enabling legislation or authorization for payment receives parliamentary approval prior to the completion of the financial statements.
- Vacation pay and compensatory leave are accrued as the benefits are earned by employees under their respective terms of employment.

- Services provided without charge by other government departments for accommodation, employer contributions to the health and dental insurance plans, worker's compensation coverage and legal services are recorded as operating expenses at their estimated cost.

(g) Employee Future Benefits

(i) Pension Benefits

Eligible civilian employees participate in the Public Service Pension Plan, a multi-employer plan administered by the Government. The Department's contributions to the Plan are charged to expenses in the year incurred and represent the total departmental obligation to the Plan. The Department's responsibility with regard to the Plan is limited to its contributions. Actuarial surpluses or deficiencies are recognized in the financial statements of the Government of Canada, as the Plan's sponsor.

DND administers pension benefits for members of the CAF. The actuarial liability and related disclosures for these benefits are presented in the financial statements of the Government of Canada and reported annually to Parliament as required by the *Canadian Forces Superannuation Act*. This differs from the accounting and disclosures of future benefits for military members presented in these financial statements whereby pension expense corresponds to the Department's annual contributions toward the cost of current and prior service, which is based on actual contributions made by members of the Plans during the period. In addition to its regular contributions, current legislation also requires the Department to make contributions for actuarial deficiencies in the Canadian Forces Pension Plan and in the Reserve Force Pension Plan, which came into force on March 1, 2007. These contributions are expensed in the year they are credited to the Plans. This accounting treatment corresponds to the funding provided to departments through Parliamentary authorities.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

(iii) Severance Benefits

Employees and CAF members entitled to severance benefits under labour contracts or conditions of employment earn these benefits as services necessary to earn them are rendered. The obligation related to the benefits earned by civilian employees is calculated using information derived from the results of the actuarially determined liability for severance benefits for the Government as a whole. The obligation related to the severance benefits earned by CAF members is based on an actuarial valuation calculated using demographic assumptions for CAF members.

(h) Accounts and Loans Receivables

Accounts and loans receivables are stated at the lower of cost and net recoverable value. Transfer payments that are unconditionally repayable are recognized as loans receivable. A valuation allowance is recorded for receivables where recovery is considered uncertain.

(i) Contingent Liabilities — Claims and Litigations

Contingent liabilities are potential liabilities, which may become actual liabilities when one or more future events occur or fail to occur. To the extent that the future event is likely to occur or fail to occur, and a reasonable estimate of the loss can be made, an estimated liability is accrued and an expense recorded. If the likelihood is not determinable the contingency is disclosed in the notes to the financial statements.

(j) Environmental Liabilities

Environmental Liabilities consist of estimated costs related to the remediation of environmentally contaminated sites as well as estimated costs related to obligations associated with future asset restoration.

- (i) Remediation Liabilities are recorded as accrued liabilities to recognize the estimated costs related to the management and remediation of contaminated sites where the Department is obligated, or likely to be obligated, to remediate the sites. If the responsibility to remediate is undeterminable, the amount is disclosed as contingent liability. If the responsibility to remediate is undeterminable and a reasonable estimate cannot be made, the nature, source and extent of contamination is disclosed as a contingent liability.
- (ii) Future Asset Restoration Obligations are recorded as accrued liabilities to recognize the estimated costs related to the restoration of tangible capital assets and the risk management of unexploded explosive ordnance (UXO) affected legacy sites. These costs are usually capitalized and amortized over the asset's estimated useful life based on obligation imposed by legislation, regulation or contractual agreement where the Department is obligated, or is likely to be obligated, to restore the tangible capital asset. If the obligation to restore the tangible capital asset is undeterminable and the estimate cannot be made, the nature and source of the potential obligation is disclosed as contingent liability.

(k) Inventories

Inventory consists of consumables (such as non-repairables, uniforms and clothing, medical and other equipment and machine tools) and ammunition (including bombs and missiles). Consumable inventories are valued using a moving weighted average price methodology. Inventory managed by contractors and not held in the Canadian Forces Supply System (CFSS) or Defence Resource Management Information System (DRMIS) is valued according to the cost method used by the contractors (first-in, first-out (FIFO), last-in, first-out (LIFO), historical cost or moving weighted average). Repairable ammunition was previously valued using a standard price and is now valued using a moving weighted average price methodology. DND is currently conducting a multi-year conversion of legacy systems into DRMIS. During the conversion process both periodic and perpetual inventory methods are being utilized. Items identified for disposal are excluded from the value of inventory as no value is expected to be recovered.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

(l) Foreign Currency Transactions

Transactions involving foreign currencies are translated into Canadian dollar equivalents using rates of exchange in effect at the time of those transactions. Monetary assets and liabilities denominated in a foreign currency are translated into Canadian dollars using the rate of exchange in effect at year-end. Gains and losses resulting from foreign currency transactions are included as revenues in Interest and Gains on Foreign Exchange in the Consolidated Statement of Operations and Departmental Net Financial Position.

(m) Tangible Capital Assets

All tangible capital assets, having an initial cost of \$30,000 or more, including capital leases, betterments and leasehold improvements, are recorded at their acquisition cost. The Department does not capitalize intangible assets, works of art and historical treasures that have cultural, aesthetic or historical value, assets located on First Nations Reserves and museum collections. Capitalization threshold values lower than \$30,000 may apply to asset pooled items (API).

Amortization of tangible capital assets is done on a straight-line basis over the estimated useful life of the capital asset as follows:

| Asset Class | Amortization Period |
|--------------------------------|---|
| Buildings | 10–40 years |
| Works | 5–40 years |
| Machinery and equipment | 3–30 years |
| Informatics hardware | 3–30 years |
| Informatics software | 2–10 years |
| Arms and weapons | 3–30 years |
| Other equipment | 5–30 years |
| Ships and boats | 10–30 years |
| Aircraft | 20–40 years |
| Non-military motor vehicles | 2–30 years |
| Military vehicles | 3–25 years |
| Other vehicles | 4–30 years |
| Leasehold improvements | Lesser of useful life of the improvement or term of lease |
| Leased tangible capital assets | Economic life or term of lease |

API are amortized at a rate consistent with the capital asset pool they support.

Assets under construction are recorded in the applicable capital asset class in the year that they become available for use and are not amortized until they become available for use.

(n) Measurement Uncertainty

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses reported in the financial statements. At the time of preparation of these statements, management believes the estimates and assumptions to be reasonable. The most significant items where estimates are used are contingent, remediation and future asset restoration liabilities, the liability for employee future benefits, allowance for doubtful accounts and the useful life of tangible capital assets. Actual results could significantly differ from those estimates. Management's estimates are reviewed periodically and, as adjustments become necessary, they are recorded in the financial statements in the year they become known.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

3. Parliamentary authorities

DND receives most of its funding through annual parliamentary authorities. Items recognized in the Consolidated Statement of Operations and Departmental Net Financial Position and the Consolidated Statement of Financial Position in one year may be funded through parliamentary authorities in prior, current or future years. Accordingly, DND has different net results of operations for the year on a government funding basis than on an accrual accounting basis. The differences are reconciled in the following tables:

(a) Reconciliation of net cost of operations to current year authorities used

| (in thousands of dollars) | 2014 | 2013 (Restated note 20) |
|--|--------------------|----------------------------|
| Net cost of operations before government funding and transfers | 17,910,121 | 20,550,999 |
| Adjustments for items affecting net cost of operations but not affecting authorities: | | |
| Amortization of tangible capital assets | (2,377,753) | (2,722,392) |
| Services provided without charge by other government departments | (733,909) | (861,165) |
| Decrease (increase) in employee future benefits | 764,626 | (44,199) |
| Refund of previous year's expenses | 85,438 | 74,963 |
| Decrease (increase) in vacation pay and compensatory leave | 16,277 | (4,484) |
| Loss on disposals of capital assets | (128,995) | (541,366) |
| Adjustments of tangible capital assets | 6,374 | (15,830) |
| Refund of program expenditures | 2,412 | 9,970 |
| Decrease in deferred revenue | 3,837 | 5,341 |
| Decrease (increase) in accrued liabilities not charged to authorities | (58,908) | 503,235 |
| Bad debt expense | (2,950) | 2,517 |
| Sale of Real Property through Canada Lands Company | 56,485 | 0 |
| Proceeds from sale of assets | 22,431 | 0 |
| Miscellaneous | 62,107 | (6,463) |
| Total items affecting net cost of operations but not affecting authorities | (2,282,528) | (3,599,873) |
| Adjustments for items not affecting net cost of operations but affecting authorities: | | |
| Acquisition of tangible capital assets | 3,012,027 | 3,008,019 |
| Decrease in lease obligations for tangible capital assets | 55,383 | 52,116 |
| Increase in inventory purchases net of usage and adjustments | 71,074 | 139,891 |
| Increase (decrease) in prepaid expenses | 13,819 | (179,073) |
| Revenues collected from prior year receivables | (15,522) | 6,111 |
| Total items not affecting net cost of operations but affecting authorities | 3,136,781 | 3,027,064 |
| Current year authorities used | 18,764,374 | 19,978,190 |



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

3. Parliamentary authorities (continued)

(b) Authorities provided and used

| (in thousands of dollars) | 2014 | 2013 |
|---|-------------------|-------------------|
| Vote 1 — Operating expenditures | 14,135,439 | 16,123,500 |
| Vote 5 — Capital expenditures | 3,618,940 | 3,322,188 |
| Vote 10 — Grants & contributions | 184,691 | 215,368 |
| Statutory amounts | 1,757,405 | 1,767,428 |
| Less: | | |
| Authorities available for future years | (836,782) | (1,135,950) |
| Frozen allotments and other planned lapses | (75,253) | (276,889) |
| Residual lapse | (20,066) | (37,455) |
| Current year authorities used | 18,764,374 | 19,978,190 |

4. Accounts payable and accrued liabilities

The following table presents details of Department's accounts payable and accrued liabilities:

| (in thousands of dollars) | 2014 | 2013 |
|--|------------------|------------------|
| Accounts payable — other government departments and agencies | 117,915 | 97,232 |
| Accounts payable — external parties | 1,280,944 | 1,390,577 |
| | 1,398,859 | 1,487,809 |
| Accrued liabilities* | 873,562 | 1,423,172 |
| Total accounts payable and accrued liabilities | 2,272,421 | 2,910,981 |

* In *Canada's Economic Action Plan 2012*, the Government announced savings measures to be implemented by departments over the next three fiscal years starting in 2012–13. As a result, department has recorded at March 31, 2014, an obligation for termination benefits for an amount of \$24.1 million (\$41.8 million 2012–13) as part of accrued liabilities to reflect the estimated workforce adjustment costs.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

5. Deposits and trust accounts

The following table presents details of Department's deposits and trust accounts:

| (in thousands of dollars) | 2014 | 2013 |
|---|--------------|--------------|
| Contractor security deposits | | |
| Deposits, beginning of year | 3,614 | 3,582 |
| Deposits received | 4,308 | 7,189 |
| Refunds | (5,334) | (7,157) |
| Contractor security deposits, end of year | 2,588 | 3,614 |
| Trust account, estates — Armed Services* | | |
| Trust account, beginning of year | 553 | 284 |
| Funds received | 1,651 | 1,815 |
| Payments | (1,447) | (1,546) |
| Trust account, estates — Armed Services, end of year | 757 | 553 |
| Closing balance | 3,345 | 4,167 |

* The Trust Account, Estates — Armed Services was established to record the service estates of deceased members of the Canadian Forces pursuant to section 42 of the *National Defence Act*. Net assets of estates are distributed to legal heirs under the administration of the Judge Advocate General, in his capacity as Director of Estates.

6. Deferred revenue

Deferred revenue represents the balance at year-end of unearned revenues stemming from amounts received from external parties which are restricted to fund the expenditures related to amounts received for fees prior to services being performed. Revenue is recognized in the period that these expenditures are incurred or the service is performed. Details of the transactions related to this account are as follows:

| (in thousands of dollars) | 2014 | 2013 |
|--|---------------|---------------|
| Foreign governments | | |
| Beginning of year | 9,794 | 16,586 |
| Funds received | (17,578) | 5,418 |
| Revenue recognized | 13,152 | (12,210) |
| Foreign governments, end of year | 5,368 | 9,794 |
| Other specified purposes | | |
| Beginning of year | 7,823 | 6,372 |
| Funds received | 591 | 1,444 |
| Revenue recognized | (2) | 7 |
| Other specified purposes, end of year | 8,412 | 7,823 |
| Closing balance | 13,780 | 17,617 |



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

7. Canadian Forces pension and insurance accounts

Established in 1901 under the *Militia Pension Act*, the present Canadian Forces pension plans (the “CF pension plans”) are administered in accordance with the provisions of the *Canadian Forces Superannuation Act*. The Canadian Forces pension plan (CFPP) covers all members of the Regular Force component of the Canadian Armed Forces. Reserve Force members who have sufficient qualifying service and pensionable earnings are members of either the CFPP or the Reserve Force pension plan (RFPP), which came into force on March 1, 2007, depending on their employment status and earnings.

The Department maintains accounts to record the transactions pertaining to the CF pension plans, which comprise the Canadian Forces Superannuation Account, the Canadian Forces Pension Fund Account, the Retirement Compensation Arrangement Account, and the Reserve Force Pension Fund Account. These accounts record transactions such as contributions, benefit payments, interest credits, refundable taxes, actuarial funding adjustments resulting from triennial reviews, and transfers to the Public Sector Pension Investment Board (PSPIB).

The value of the liabilities reported in these financial statements for the CF pension plans reflect only the balances which are posted in the departmental financial system. These balances do not include the actuarial value of the liabilities determined by the Chief Actuary of the Office of the Superintendent of Financial Institutions nor the details of the investments that are held by PSPIB. Additional information on the CF pension plans, including audited financial statements, is published in the Annual Report of the Canadian Forces pension plans, which is available through the Department of National Defence Website. For further information on PSPIB, please visit their website www.pspib.ca.

The Department also maintains the Regular Forces Death Benefit Account, which provides life insurance to contributing members and former members of the Canadian Armed Forces. This account records contributions, premiums, interest, and benefit payments.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

7. Canadian Forces pension and insurance accounts (continued)

The following table provides details of the Canadian Forces pension and insurance accounts:

| (in thousands of dollars) | 2014 | 2013 |
|--|-------------------|-------------------|
| Canadian Forces Superannuation Account | | |
| Beginning of year | 46,357,136 | 46,269,146 |
| Funds received and other credits | 2,434,150 | 2,558,251 |
| Payments and other charges | (2,493,910) | (2,470,261) |
| Canadian Forces Superannuation Account, end of year | 46,297,376 | 46,357,136 |
| Canadian Forces Pension Fund Account | | |
| Beginning of year | 276,096 | 280,497 |
| Funds received and other credits | 1,508,486 | 1,479,324 |
| Payments and other charges | (511,388) | (428,566) |
| Transfers to the Public Sector Pension Investment Board | (1,009,839) | (1,055,159) |
| Canadian Forces Pension Fund Account, end of year | 263,355 | 276,096 |
| Reserve Force Pension Fund Account | | |
| Beginning of year | 13,234 | 9,725 |
| Funds received and other credits | 40,242 | 41,256 |
| Payments and other charges | (51,867) | (37,747) |
| Reserve Force Pension Fund Account, end of year | 1,609 | 13,234 |
| Retirement Compensation Arrangements Account* | | |
| Beginning of year | 329,951 | 307,572 |
| Funds received and other credits | 49,047 | 49,339 |
| Payments and other charges | (27,812) | (26,960) |
| Retirement Compensation Arrangements Account, end of year | 351,186 | 329,951 |
| Regular Force Death Benefit Account | | |
| Beginning of year | 191,562 | 190,303 |
| Funds received and other credits | 30,103 | 29,903 |
| Payments and other charges | (32,413) | (28,644) |
| Regular Force Death Benefit Account, end of year | 189,252 | 191,562 |
| | 47,102,778 | 47,167,979 |

* The Retirement Compensation Arrangements (RCA) account records transactions for pension benefits that are provided in excess of those permitted under the *Income Tax Act*. The RCA is registered with Canada Revenue Agency (CRA) and a transfer is made annually between the RCA Account and CRA to either remit a 50-percent refundable tax in respect of the net contributions and interest credits or to be credited a reimbursement based on the net benefit payments. As at March 31, 2014, the total refundable tax transferred amounts to \$341 million (\$319 million in 2012-13).



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

8. Lease obligations for tangible capital assets

The Department has entered into agreements to lease certain equipment under capital leases with a cost of \$836 million and accumulated amortization of \$536 million as at March 31, 2014 (\$870 million and \$518 million respectively as at March 31, 2013). The obligations for the upcoming years include the following:

| (in thousands of dollars) | Total future minimum lease payments | Imputed interest (5.29% to 8.05%) | Balance of obligations 2014 | Balance of obligations 2013 |
|---------------------------|-------------------------------------|-----------------------------------|-----------------------------|-----------------------------|
| Buildings | 130,960 | (37,230) | 93,730 | 100,309 |
| Aircraft | 392,778 | (61,502) | 331,276 | 380,080 |
| | 523,738 | (98,732) | 425,006 | 480,389 |

Future minimum lease payments

| (in thousands of dollars) | 2014–2015 | 2015–2016 | 2016–2017 | 2017–2018 | 2018–19 and thereafter |
|---------------------------|---------------|---------------|---------------|---------------|------------------------|
| Buildings | 12,059 | 12,000 | 11,937 | 11,867 | 83,099 |
| Aircraft | 70,105 | 70,105 | 70,105 | 70,105 | 112,358 |
| | 82,164 | 82,105 | 82,042 | 81,972 | 195,457 |

The Department has entered into agreements for buildings and aircraft under capital leases (refer to note 14 of these financial statements).



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

9. Employee future benefits

(a) Pension benefits:

i) The Department's Public Service employees participate in the Public Service Pension Plan (the Plan), which is sponsored and administered by the Government of Canada. Pension benefits accrue up to a maximum of 35 years at a rate of 2 percent per year of pensionable service, times the average of the best five consecutive years of earnings. The benefits are integrated with Canada/Québec Pension Plan benefits and they are indexed to inflation.

Both the employees and the Department contribute to the cost of the Plan. Due to the amendment of the *Public Service Superannuation Act* following the implementation of provisions related to *Canada's Economic Action Plan 2012*, employee contributions have been divided into two groups — Group 1 relates to existing plan members as of December 31, 2012 and Group 2 relates to members joining the Plan as of January 1, 2013. Each group has a distinct contribution rate.

The 2013–14 expense amounts to \$207.9 million (\$215.7 million in 2012–13). For Group 1 members, the expense represents approximately 1.6 times (1.7 times in 2012–13) the employees contributions and, for Group 2 members, approximately 1.5 times (1.6 times in 2012–13) the employees contributions.

The Department's responsibility with regard to the pension plan is limited to its contributions. Actuarial surpluses or deficiencies are recognized in the financial statements of the Government of Canada, as the Plan's sponsor.

ii) The members of the Canadian Armed Forces Regular Force and eligible members of the Reserve Force participate in the Canadian Forces pension plan, which is sponsored by the Government of Canada and administered by the Department. Pension benefits accrue up to a maximum of 35 years at a rate of 2 percent per year of pensionable service, times the average of the best five consecutive years of earnings. The benefits are integrated with Canada/Québec Pension Plan benefits and are indexed to inflation.

iii) The members of the Canadian Armed Forces Reserve Force pension plan who are not eligible for participation in the Canadian Forces pension plan, may be eligible to participate in the Reserve Force pension plan, which is sponsored by the Government of Canada and administered by the Department. Pension benefits accrue at a rate of 1.5 percent of pensionable earnings during the member's service, plus an additional 0.5 percent times the average of the best five consecutive years of earnings for those members who are not yet eligible for Canada/Québec Pension Plan benefits. The benefits are integrated with Canada/Québec Pension Plan benefits and are indexed to inflation.

Both the members and the Department contribute to the cost of the CF pension plans for both current and prior service. The 2013–14 expense amounts to \$1,133.2 million (\$1,140.7 million in 2012–13), which represents approximately 2.12 times (2.3 times in 2012–13) the contributions by employees.

The Department is responsible for providing program management and the day-to-day administration of the CF pension plans. The actuarial liability and actuarial surpluses or deficiencies are recognized in the financial statements of the Government of Canada, as the Plans' sponsor.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

9. Employee future benefits (continued)

As a result of the actuarial funding report by the Office of the Chief Actuary, the President of Treasury Board has approved:

- Annual actuarial adjustments of \$249 million (\$249 million in 2012–13) to fund the deficit in the Canadian Forces Pension Fund Account, until the deficit is funded as per the triennial funding valuation; and
- A government contribution holiday to the Reserve Force Pension Fund Account starting in November 2011, to reduce the non-permitted surplus in the account. Government contributions will resume when the non-permitted surplus is reduced as per the triennial funding valuation.

For more information on these adjustments, please consult the actuarial reports, available at the Office of the Chief Actuary's website (<http://www.osfi-bsif.gc.ca>)

(b) Severance benefits:

The Department provides severance benefits to its public service employees and CAF members based on eligibility, years of service, final salary and authorized period of service. These severance benefits are not pre-funded. Benefits will be paid from future authorities.

As part of collective agreement negotiations with certain employee groups, and changes to conditions of employment for executives and certain non-represented employees, the accumulation of severance benefits under the employee severance pay program ceased for these employees commencing in 2012. Employees subject to these changes have been given the option to be immediately paid the full or partial value of benefits earned to date or collect the full or remaining value of benefits on termination from the public service. These changes have been reflected in the calculation of the outstanding severance benefit obligation disclosed below.

Information about the severance benefits, measured as at March 31, is as follows:

| (in thousands of dollars) | 2014 | 2013 |
|--|------------------|------------------|
| Public Service Employees | | |
| Accrued benefit obligation, beginning of year | 165,258 | 222,459 |
| Expenses for the year | 50,495 | 46,393 |
| Benefits paid during the year | (127,901) | (103,594) |
| Accrued benefit obligation, end of year | 87,852 | 165,258 |
| Canadian Armed Forces Members | | |
| Accrued benefit obligation, beginning of year | 1,608,100 | 1,506,700 |
| Expenses for the year | (568,096) | 722,083 |
| Benefits paid during the year | (119,124) | (620,683) |
| Accrued benefit obligation, end of year | 920,880 | 1,608,100 |
| Total accrued benefit obligation, end of year | 1,008,732 | 1,773,358 |



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

10. Accounts receivables

The following table presents details of accounts receivable:

| (in thousands of dollars) | 2014 | 2013 |
|---|----------------|----------------|
| External parties | 79,365 | 63,854 |
| Other government departments and agencies | 817,637 | 131,670 |
| | 897,002 | 195,524 |
| Less: allowance for doubtful accounts on external receivables | 8,181 | 5,892 |
| Gross accounts receivable | 888,821 | 189,632 |
| Accounts receivable held on behalf of Government | (2,703) | (2,080) |
| Net Receivables | 886,118 | 187,552 |

11. Loans and advances

The following table presents details of loans and advances:

| (in thousands of dollars) | 2014 | 2013 |
|---|---------------|---------------|
| Imprest accounts, standing advances and authorized loans to CAF members | 40,875 | 34,781 |
| Accountable advances (temporary advances) | 0 | 12 |
| Total loans and advances | 40,875 | 34,793 |

12. Prepaid expenses

The following is a breakdown of prepaid expenses:

| (in thousands of dollars) | 2014 | 2013 |
|---|----------------|----------------|
| Foreign military purchases | 323,447 | 420,456 |
| Mercury Global Military Wideband Satellite Communications Project | 86,593 | 0 |
| NATO flying training Canada (NFTC) | 51,397 | 48,923 |
| Sea sparrow missiles | 35,227 | 18,985 |
| Building rentals | 18,505 | 11,308 |
| Joint strike fighter development | 0 | 6,018 |
| Other purchases | 108,672 | 104,332 |
| Total prepaid expenses | 623,841 | 610,022 |



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

13. Inventories

The following table presents the details of inventory, measured at cost using the weighted moving average method:

| (in thousands of dollars) | 2014 | 2013 (Restated note 20) |
|---|------------------|----------------------------|
| Ammunition, bombs and missiles | 3,553,220 | 3,601,424 |
| Contractor held inventory | 472,505 | 377,526 |
| Uniforms and clothing | 431,862 | 504,930 |
| Metal | 327,246 | 321,187 |
| Engineering, test and technical equipment and machine tools | 288,106 | 257,946 |
| Communication, electrical parts/accessories and informatics equipment | 263,426 | 282,106 |
| Ship spares | 249,238 | 229,364 |
| Land equipment spares | 184,473 | 246,304 |
| Sonobuoys, parts and accessories | 148,705 | 113,498 |
| Aircraft spares | 135,980 | 77,410 |
| Medical equipment | 109,038 | 117,326 |
| Fuel, petroleum and oil | 63,775 | 64,065 |
| Miscellaneous | 202,195 | 165,609 |
| Total inventories | 6,429,769 | 6,358,695 |

The cost of consumed inventory recognized as an expense in the Consolidated Statement of Operations and Departmental Net Financial Position is \$480 million in 2013-14 (\$699 million in 2012-13-restated).



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

14. Tangible capital assets

| Cost | | | | | |
|---------------------------------------|--|----------------------------|------------------|--------------------------|---------------------|
| (in thousands of dollars) | Balance beginning of year (Restated note 20) | Adjustments ⁽¹⁾ | Acquisitions | Disposals and write-offs | Balance end of year |
| Land, buildings and works | | | | | |
| Land | 85,185 | (1,093) | 3,885 | (185) | 87,792 |
| Buildings | 8,157,896 | 542,302 | 2,060 | (16,214) | 8,686,044 |
| Works | 2,314,272 | 121,719 | 68 | (46,045) | 2,390,014 |
| | 10,557,353 | 662,928 | 6,013 | (62,444) | 11,163,850 |
| Machinery and equipment | | | | | |
| Machinery and equipment | 6,887,409 | 422,789 | 106,015 | (642,963) | 6,773,250 |
| Informatics hardware | 6,859,225 | 578,514 | 70,877 | (564,778) | 6,943,838 |
| Informatics software | 611,556 | 140,578 | 0 | 0 | 752,134 |
| Arms and weapons | 6,296,480 | 294,786 | 60,445 | (421,726) | 6,229,985 |
| Other equipment | 88,388 | 17,098 | 643 | (1,915) | 104,214 |
| | 20,743,058 | 1,453,765 | 237,980 | (1,631,382) | 20,803,421 |
| Ships, aircraft and vehicles | | | | | |
| Ships and boats | 11,891,494 | 124,109 | 62,626 | (126,684) | 11,951,545 |
| Aircraft | 15,182,642 | 1,304,546 | 300,049 | (295,803) | 16,491,434 |
| Non-military motor vehicles | 792,415 | 8,976 | 61,638 | (35,817) | 827,212 |
| Military vehicles | 1,797,125 | 6,194 | 9,862 | (42,947) | 1,770,234 |
| Other vehicles | 420,623 | 7,695 | 14,244 | (26,141) | 416,421 |
| | 30,084,299 | 1,451,520 | 448,419 | (527,392) | 31,456,846 |
| Leasehold improvements | | | | | |
| Leasehold improvements | 41,735 | 146 | 0 | 0 | 41,881 |
| | 41,735 | 146 | 0 | 0 | 41,881 |
| Leased tangible capital assets | | | | | |
| Buildings | 139,004 | (64) | 0 | 0 | 138,940 |
| Other equipment | 48 | 0 | 0 | 0 | 48 |
| Aircraft | 731,130 | 0 | 0 | (34,254) | 696,876 |
| | 870,182 | (64) | 0 | (34,254) | 835,864 |
| Assets under construction | | | | | |
| Buildings | 960,164 | (513,581) | 559,944 | 0 | 1,006,527 |
| Engineering works | 164,212 | (151,100) | 79,472 | 0 | 92,584 |
| Informatics software | 514,751 | (197,601) | 55,460 | 0 | 372,610 |
| Equipment | 6,502,013 | (1,775,289) | 1,624,739 | (33,619) | 6,317,844 |
| | 8,141,140 | (2,637,571) | 2,319,615 | (33,619) | 7,789,565 |
| Gross tangible capital assets | 70,437,767 | 930,724 | 3,012,027 | (2,289,091) | 72,091,427 |

(1) Adjustments represent transfers, adjustments to asset pooled items (API), assets under construction (AUC) put into use and reclassifications.

During 2013-14, the Department transferred out land with a net book value of \$1,093,012 to Communications Security Establishment Canada, a vehicle to Justice Canada with a net book value of \$1 and machinery and equipment to Transport Canada with a net book value of \$20,977. Also during 2013-14 the Department transferred in vehicles with a book value of \$32,966 from Justice Canada and Canadian Security Intelligence Service and machinery and equipment with a net book value of \$1 from Industry Canada. These transfers are included in the adjustments column.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

14. Tangible capital assets (continued)

| Accumulated amortization | | | | | | | |
|---------------------------------------|--|----------------|------------------|--------------------------|---------------------|-------------------|-------------------------|
| (in thousands of dollars) | Balance beginning of year (Restated note 20) | Adjustments | Amortization | Disposals and write-offs | Balance end of year | Net Book Value | |
| | | | | | | 2014 | 2013 (Restated Note 20) |
| Land, buildings and works | | | | | | | |
| Land | | | | | | 87,792 | 85,185 |
| Buildings | 3,558,442 | 0 | 217,637 | [10,836] | 3,765,243 | 4,920,801 | 4,599,454 |
| Works | 1,284,618 | 0 | 68,951 | [22,945] | 1,330,624 | 1,059,390 | 1,029,654 |
| | 4,843,060 | 0 | 286,588 | [33,781] | 5,095,867 | 6,067,983 | 5,714,293 |
| Machinery and equipment | | | | | | | |
| Machinery and equipment | 5,183,251 | 314,447 | 165,342 | [641,206] | 5,021,834 | 1,751,416 | 1,704,158 |
| Informatics hardware | 5,695,645 | 313,525 | 344,600 | [564,728] | 5,789,042 | 1,154,796 | 1,163,580 |
| Informatics software | 341,507 | 0 | 56,090 | 0 | 397,597 | 354,540 | 270,051 |
| Arms and weapons | 3,707,221 | 165,237 | 212,213 | [355,021] | 3,729,650 | 2,500,335 | 2,589,259 |
| Other equipment | 59,529 | 1,482 | 6,459 | [1,870] | 65,600 | 38,614 | 28,859 |
| | 14,987,153 | 794,691 | 784,704 | [1,562,825] | 15,003,723 | 5,799,701 | 5,755,907 |
| Ships, aircraft and vehicles | | | | | | | |
| Ships and boats | 7,528,036 | [30,743] | 506,696 | [123,351] | 7,880,638 | 4,070,907 | 4,363,458 |
| Aircraft | 8,759,823 | 146,002 | 637,972 | [306,199] | 9,237,598 | 7,253,836 | 6,422,819 |
| Non-military motor vehicles | 520,709 | 3,256 | 41,043 | [35,324] | 529,684 | 297,528 | 271,706 |
| Military vehicles | 1,220,983 | 5,322 | 72,210 | [38,774] | 1,259,741 | 510,493 | 576,142 |
| Other vehicles | 285,924 | 6,902 | 14,382 | [26,110] | 281,098 | 135,323 | 134,699 |
| | 18,315,475 | 130,739 | 1,272,303 | [529,758] | 19,188,759 | 12,268,087 | 11,768,824 |
| Leasehold improvements | | | | | | | |
| Leasehold improvements | 19,472 | 39 | 4,378 | 0 | 23,889 | 17,991 | 22,263 |
| | 19,472 | 39 | 4,378 | 0 | 23,889 | 17,991 | 22,263 |
| Leased tangible capital assets | | | | | | | |
| Buildings | 60,749 | [37] | 6,286 | 0 | 66,998 | 71,942 | 78,255 |
| Other equipment | 41 | 0 | 5 | 0 | 46 | 2 | 7 |
| Aircraft | 457,238 | [1] | 23,489 | [11,301] | 469,425 | 227,451 | 273,892 |
| | 518,028 | [38] | 29,780 | [11,301] | 536,469 | 299,395 | 352,154 |
| Assets under construction | | | | | | | |
| Buildings | | | | | | 1,006,527 | 960,164 |
| Engineering works | | | | | | 92,584 | 164,212 |
| Informatics software | | | | | | 372,610 | 514,751 |
| Equipment | | | | | | 6,317,845 | 6,502,013 |
| | | | | | | 7,789,565 | 8,141,140 |
| Total | 38,683,188 | 925,431 | 2,377,753 | [2,137,665] | 39,848,708 | 32,242,722 | 31,754,581 |

In 2013–14, the Department had capital asset holdings that were damaged but that have yet to be approved for write-down or write-off. The estimated net book value of these holdings is disclosed in the table on the right.

Further evaluation of these capital asset holdings will be conducted in fiscal year 2014–15 and, once the review is completed and the net book value of these holdings is confirmed, the applicable write-down or write-off accounting entries will be recorded.

| | 2014 | 2013 |
|----------------------------|-----------------|-----------------|
| Assets likely for disposal | \$ 19.3 million | \$ 32.9 million |
| Assets pending evaluation | \$ 0.4 million | \$ 3.7 million |
| Assets under repair | \$ 8.3 million | \$ 3.7 million |



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

15. Contingent liabilities

Contingent liabilities arise in the normal course of the operations of the Department and their ultimate disposition is unknown. The Department is involved in three categories of contingent liabilities: claims and litigations, remediation liabilities, and future asset restoration liabilities.

(a) Claims and litigations

Claims have been made against the Department in the normal course of operations. These claims include items with pleading amounts and others for which no amount is specified. While the total amount claimed in these actions is significant, their outcomes are not determinable. The Department has recorded an allowance for claims and litigations where it is likely that there will be a future payment and a reasonable estimate of the loss can be made. Claims and litigations for which the outcome is not determinable and a reasonable estimate can be made by management amount to approximately \$12.6 million (\$33.9 million in 2012–13) at March 31, 2014.

(b) Remediation liabilities — contaminated sites

Liabilities are accrued to record the estimated costs related to the management and remediation of environmentally contaminated sites where the Department is obligated or likely to be obligated to incur such costs.

Liability estimates are based on information known at a given point in time. These estimates are subject to variability due to: professional judgment involved in developing estimates, the possibility that additional volumes of contaminated media may be discovered upon implementation of the remedial action plan, and/or new technologies becoming available during the course of implementing the remedial action plan.

The Department has identified approximately 242 sites (277 sites in 2012–13) where the Department is obligated or likely to be obligated, to remediate. The Department recorded a remediation liability of \$462.4 million (\$407.1 million in 2012–13) for these sites.

A contingent liability exists when the responsibility of the Government for remediation is unconfirmed. Additionally, a contingent liability related to measurement uncertainty should only be disclosed when it is expected to be resolved within a year. Using this criteria, no contingent liabilities are being disclosed in 2013–14. In 2012–13, \$224.8 million was disclosed as contingent liabilities, although this amount was related to measurement uncertainty which was not expected to be resolved within one year.

There are 3 contaminated sites in Valcartier that have measurement uncertainty with a possible range of cost estimates between \$4.1 million and \$9.6 million. A closing liability for these 3 sites has been recorded at \$6.9 million. The measurement uncertainty will be resolved by the close of next fiscal year, once the remediation work progresses at which time the most reasonable estimate can be confirmed.

In 2013–14, the Department continued developing options (as part of the Esquimalt Harbour Remediation Project) to reduce the ecological and human health risks associated with contaminated sediments in Esquimalt Harbour.

The overall liability for Goose Bay was reduced due to the completion of remedial work, and a number of decisions in 2013–14 based on applying risk management principles to sites.

The DEW Line Clean Up project has largely completed the remediation phase. However at 4 of the 21 sites, there remains some hazardous waste removal and site demobilization.

As a result of recent site assessment activities, the Department has recognized a \$5.0 million contaminated site liability for the divestiture of its site at Niagara-on-the-Lake Rifle Range.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

15. Contingent liabilities (continued)

In 2012–13 a liability was recognized for the trichloroethylene (TCE) groundwater contamination at CFB Valcartier. There is potential for changes to this liability given the long duration of the groundwater pump and treat solution (15+ years) and remaining uncertainties regarding approach to deal with the source contamination. The cost estimates will continue to be reviewed at least annually and adjusted as necessary.

As knowledge increases about the impacts of contaminants on human health and the environment, new clean up criteria for emerging contaminants may be introduced and existing guidelines for known contaminants may be updated or revised. New or changed criteria have the potential to increase liability for the Department. One group of emerging contaminants is perfluorinated compounds (PFCs) which has been found at several current and former federal sites.

A potential obligation exists for environmental mitigation at Camp Ipperwash. The uncertainty related to this potential liability will be resolved once environmental investigations have been completed and clean-up options have been developed. These investigations are expected to continue until 2017–18.

During 2013–14, assessment activities were undertaken at 121 suspected or confirmed contaminated sites with expenditures of \$4.0 million. As a result of assessment activities, additional liabilities may be reported in the future.

(c) Future Asset Restoration Liability

UXO Affected Legacy Sites

The Department has identified approximately 865 unexploded explosive ordnance (UXO) suspected sites, for which clearance action may be necessary. Of these the Department has recorded \$2.0 million in liabilities (\$3.0 million in 2012–13) related to 6 out of a total of 63 unexploded explosive ordnance sites (8 out of 50 sites, in 2012–13) where clearance action is likely.

The basis for the currently identified liability for Lac St. Pierre has been reviewed and remains unchanged from last year. It is possible that the amount will change once UXO mitigation and clearance options have been further developed.

An obligation exists for UXO risk mitigation at the former Sarcee Training Area in Calgary. This obligation cannot yet be recognized as a future asset restoration liability due to uncertainty regarding the scope and cost of the UXO risk mitigation strategy. The uncertainty will be resolved once UXO investigations have been completed and mitigation options have been developed.

Potential obligations exist for UXO risk mitigation at the former military properties in the Vernon area. These obligations cannot yet be recognized as a future asset restoration liability due to uncertainty regarding the scope and cost of potential UXO risk mitigation strategies. These uncertainties will be resolved once UXO investigations have been completed and mitigation options have been developed.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

15. Contingent liabilities (continued)

Real Property Liabilities

In addition to the liabilities related to UXO affected legacy sites, there are potential obligations related to real property. These obligations may arise from property disposal transactions, termination of lease agreements, oil and gas activities on DND/CF property, and other transactions.

The Department will be transferring the administration of approximately 50 hectares of land at Beecher's Bay, BC to Aboriginal Affairs and Northern Development Canada. The Department retains responsibility, and research has shown that the risk of UXO presence is low.

A potential obligation exists for UXO risk mitigation at Camp Ipperwash. The uncertainty will be resolved once UXO investigations have been completed and clearance options have been developed. These UXO investigations are expected to continue until 2015–16, at which time a reasonable estimate will be available.

The Niagara-on-the-Lake range was closed in 2000 as it was no longer required by the Department for operations. The property is owned by Parks Canada and, according to the lease agreement the property must be free of contamination before the lease agreement can be terminated. Previous investigations confirmed that parts of the property are affected by UXO, but further assessment is necessary. Once the assessment is completed, and a final land use is determined, the Department will be better able to determine and estimate its liability.

A potential obligation exists for abandoned wells associated with oil and gas activities at CFB Suffield, however the extent of this obligation is not known at this time. The uncertainty will be resolved once the departmental research into provincial, federal and industry standards and obligations is completed. This research will continue through 2014–15.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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16. Contractual obligations

The nature of the Department's activities can result in some large multi-year contracts and obligations whereby the Department will be obligated to make future payments when the services/goods are received. Contractual obligations over \$10 million that can be reasonably estimated are summarized as follows:

| (in thousands of dollars) | 2014–2015 | 2015–2016 | 2016–2017 | 2017–2018 | 2018–2019 and thereafter | Total |
|---------------------------|------------------|------------------|------------------|------------------|--------------------------------|-------------------|
| Fixed Assets | 1,470,854 | 1,289,755 | 453,038 | 185,150 | 941,246 | 4,340,043 |
| Purchases | 2,076,432 | 1,324,264 | 1,160,017 | 852,080 | 4,036,186 | 9,448,979 |
| Total | 3,547,286 | 2,614,019 | 1,613,055 | 1,037,230 | 4,977,432 | 13,789,022 |

17. Related party transactions

The Department is related as a result of common ownership to all Government departments, agencies and Crown Corporations. The Department enters into transactions with these entities in the normal course of business and on normal trade terms. During the year, the Department received common services which were obtained without charge from other Government departments as disclosed below.

(a) Common services provided without charge by other government departments

During the year, the Department received services without charge from certain common service organizations, related to accommodation, legal services, the employer's contribution to the health and dental insurance plans and workers' compensation coverage. These services provided without charge have been recorded in the Department's Statement of Operations and Departmental Net Financial Position as follows:

| (in thousands of dollars) | 2014 | 2013 |
|--|----------------|----------------|
| Employer's contributions to the health and dental plans paid by Treasury Board of Canada Secretariat | 647,303 | 776,994 |
| Accommodation provided by Public Works and Government Services Canada | 74,159 | 72,093 |
| Worker's compensation coverage provided by Employment and Social Development Canada | 8,848 | 8,746 |
| Legal services provided by Department of Justice Canada | 3,599 | 3,332 |
| Total | 733,909 | 861,165 |

The Government has centralized some of its administrative activities for efficiency, cost-effectiveness purposes and economic delivery of programs to the public. As a result, the Government uses central agencies and common service organizations so that one department performs services for all other departments and agencies without charge. The costs of these services, such as the payroll and cheque issuance services provided by Public Works and Government Services of Canada and audit services provided by the Office of the Auditor General are not included in the Department's Consolidated Statement of Operations and Departmental Net Financial Position. The costs of information technology infrastructure services provided by Shared Services Canada, following the transfer of responsibilities in November 2011 and April 2013, are also not included in the Department's Consolidated Statement of Operations and Departmental Net Financial Position.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

17. Related party transactions (continued)

(b) Other transactions with related parties

| (in thousands of dollars) | 2014 | 2013 |
|--|------------------|------------------|
| Expenses — other government departments and agencies | 1,089,882 | 2,458,418 |
| Revenues — other government departments and agencies | 77,957 | 14,709 |
| Total | 1,167,839 | 2,473,127 |

Expenses and revenues disclosed in (b) exclude common services provided without charge, which are already disclosed in (a).

18. Transfers to other government departments

On April 3, 2013, the Department transferred responsibility for the acquisition and provision of hardware and software, including security software, for workplace technology devices to Shared Services Canada pursuant to Order-in-Council 2013-0368, including the stewardship responsibility for the assets and liabilities related to the program. The 2013 comparative figures have been reclassified on the Statement of Operations and Departmental Net Financial Position to present the expenses of the transferred operations. During the transition period, the Department continued to administer the transferred activities on behalf of Shared Services Canada. The administered expenses amounted to \$18.1 million for the year. These expenses are not recorded in these financial statements.

19. Segmented information

Presentation by segment is based on the Department's Program Alignment Architecture. The presentation by segment is based on the same accounting policies as described in the summary of significant accounting policies in note 2. The following table presents the expenses incurred and revenues generated for the main program, by major object of expenses and by major type of revenues. The segment results for the period are as follows:



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

19. Segmented information (continued)

| (in thousands of dollars) | DST | RPIT | EAD | RPIAD |
|--|----------------|------------------|------------------|----------------|
| Operating expense | | | | |
| Salary and employee benefits | 198,343 | 947,614 | 196,583 | 16,485 |
| Amortization | 320 | 0 | 2,078,174 | 289,411 |
| Professional and special services | 59,298 | 50,165 | 460,231 | 64,082 |
| Repair and maintenance | 4,505 | 151 | 157,842 | 1,323 |
| Transportation and communication | 8,013 | 22,548 | 16,996 | 970 |
| Materials and supplies | 8,596 | 28,747 | 4,371 | 2,163 |
| Expenses related to tangible assets | 9,597 | 2,276 | 253,745 | 78,579 |
| Other services | 14,209 | 5,427 | 37,269 | 1,265 |
| Other expenses | (53,130) | 17,368 | (1,022,645) | (83,056) |
| Accommodation | 2,547 | 11,069 | 8,693 | 2,924 |
| Utilities | 4,053 | 2 | 3 | 388 |
| Equipment and other rentals | 556 | 2,343 | 2,942 | 58 |
| Loss on disposals and write-offs and write-downs of assets | 128,995 | 0 | 0 | 0 |
| Interest on capital lease payments | 41 | 44,867 | (49,565) | (6,661) |
| Advertising, printing and related services | 821 | 5,310 | 448 | 1 |
| Bad debts | 55 | 326 | 73 | 6 |
| Total operating expenses | 386,819 | 1,138,213 | 2,145,160 | 367,938 |
| Transfer payments | | | | |
| Transfers to other countries and international organizations | 0 | 0 | (371) | 0 |
| Transfers to individuals | 0 | 0 | 0 | 1,024 |
| Transfers to other levels of government | 123 | 0 | 0 | 0 |
| Transfers to non-profit organizations | 0 | 0 | 0 | 0 |
| Total transfer payments | 123 | 0 | (371) | 1,024 |
| Total expenses | 386,942 | 1,138,213 | 2,144,789 | 368,962 |
| Revenues | | | | |
| Sale of goods and services | 1,071 | 2,042 | 162 | 165 |
| Gains on disposals of assets | 85 | 10 | 2,865 | 0 |
| Other | 147 | 2 | (23) | 1 |
| Interest and gains on foreign exchange | 33 | 2 | 3,335 | 1 |
| Revenues earned on behalf of Government | (450) | 0 | (174) | 0 |
| Total revenues | 886 | 2,056 | 6,165 | 167 |
| Net cost from continuing operations | 386,056 | 1,136,157 | 2,138,624 | 368,795 |

DST Defence Science and Technology
 RPIT Recruiting of Personnel and Initial Training
 EAD Equipment Acquisition and Disposal
 RPIAD Real Property Infrastructure Acquisition and Disposal



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

19. Segmented information (continued)

| (in thousands of dollars) | MR | LR | AR | JCR |
|--|------------------|------------------|------------------|------------------|
| Operating expense | | | | |
| Salary and employee benefits | 1,325,966 | 2,390,726 | 1,096,532 | 1,069,043 |
| Amortization | 0 | 0 | 0 | 2,418 |
| Professional and special services | 267,679 | 164,951 | 107,437 | 210,088 |
| Repair and maintenance | 83,302 | 175,880 | 254,057 | 71,297 |
| Transportation and communication | 18,578 | 61,462 | 42,230 | 79,089 |
| Materials and supplies | 65,830 | 95,083 | 63,605 | 215,548 |
| Expenses related to tangible assets | 51,207 | 61,955 | 27,178 | 39,684 |
| Other services | 8,691 | 42,680 | 23,172 | 45,899 |
| Other expenses | 489,850 | 266,340 | 279,287 | 82,734 |
| Accommodation | 11,524 | 24,056 | 9,724 | 39,295 |
| Utilities | 30,957 | 54,087 | 27,564 | 28,787 |
| Equipment and other rentals | 17,472 | 36,156 | 31,084 | 18,174 |
| Loss on disposals and write-offs and write-downs of assets | 0 | 0 | 0 | 0 |
| Interest on capital lease payments | 82 | 2,935 | 41 | 8,598 |
| Advertising, printing and related services | 191 | 468 | 602 | 2,098 |
| Bad debts | 382 | 641 | 310 | 329 |
| Total operating expenses | 2,371,711 | 3,377,420 | 1,962,823 | 1,913,081 |
| Transfer payments | | | | |
| Transfers to other countries and international organizations | (214) | 0 | 0 | 0 |
| Transfers to individuals | 0 | 0 | 0 | 0 |
| Transfers to other levels of government | 0 | 0 | 0 | 700 |
| Transfers to non-profit organizations | 0 | 0 | 0 | 0 |
| Total transfer payments | (214) | 0 | 0 | 700 |
| Total expenses | 2,371,497 | 3,377,420 | 1,962,823 | 1,913,781 |
| Revenues | | | | |
| Sale of goods and services | 20,636 | 25,748 | 16,036 | 15,774 |
| Gains on disposals of assets | 1,814 | 2,633 | 994 | 887 |
| Other | 646 | 402 | 311 | 1,399 |
| Interest and gains on foreign exchange | 339 | 234 | 374 | 135 |
| Revenues earned on behalf of Government | (466) | 16 | 8 | 6 |
| Total revenues | 22,969 | 29,033 | 17,723 | 18,201 |
| Net cost from continuing operations | 2,348,528 | 3,348,387 | 1,945,100 | 1,895,580 |

MR Maritime Readiness
 LR Land Readiness
 AR Aerospace Readiness
 JCR Joint and Common Readiness



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

19. Segmented information (continued)

| (in thousands of dollars) | SA | CaPSS | CoPSS | IPSS |
|--|----------------|----------------|----------------|------------------|
| Operating expense | | | | |
| Salary and employee benefits | 235,919 | 121,786 | 86,575 | 619,952 |
| Amortization | 0 | 0 | 0 | 0 |
| Professional and special services | 29,048 | 6,635 | 4,636 | 82,128 |
| Repair and maintenance | 36,353 | 117,463 | 76,481 | 45,715 |
| Transportation and communication | 7,106 | 8,303 | 5,121 | 36,865 |
| Materials and supplies | 8,781 | 26,437 | 13,992 | 128,619 |
| Expenses related to tangible assets | 9,083 | 4,125 | 603 | 14,587 |
| Other services | 14,352 | 5,011 | 1,495 | 14,510 |
| Other expenses | 27,698 | 53,965 | 21,491 | 100,023 |
| Accommodation | 2,492 | 1,406 | 1,769 | 8,203 |
| Utilities | 1,032 | 13 | 3,979 | 3,905 |
| Equipment and other rentals | 504 | 4,246 | 1,508 | 25,252 |
| Loss on disposals and write-offs and write-downs of assets | 0 | 0 | 0 | 0 |
| Interest on capital lease payments | 0 | 0 | 0 | 25,238 |
| Advertising, printing and related services | 364 | 65 | 4 | 133 |
| Bad debts | 123 | 62 | 22 | 215 |
| Total operating expenses | 372,855 | 349,517 | 217,676 | 1,105,345 |
| Transfer payments | | | | |
| Transfers to other countries and international organizations | 0 | 190 | 0 | 147,793 |
| Transfers to individuals | 0 | 5,690 | 0 | 0 |
| Transfers to other levels of government | 0 | 2,773 | 0 | 0 |
| Transfers to non-profit organizations | 0 | 0 | 0 | 0 |
| Total transfer payments | 0 | 8,653 | 0 | 147,793 |
| Total expenses | 372,855 | 358,170 | 217,676 | 1,253,138 |
| Revenues | | | | |
| Sale of goods and services | 396 | 666 | 854 | 154,529 |
| Gains on disposals of assets | 2 | 2 | 0 | 10,230 |
| Other | 15 | 0 | 40 | 392 |
| Interest and gains on foreign exchange | 129 | 13 | 82 | 520 |
| Revenues earned on behalf of Government | 0 | 0 | 0 | 0 |
| Total revenues | 542 | 681 | 976 | 165,671 |
| Net cost from continuing operations | 372,313 | 357,489 | 216,700 | 1,087,467 |

SA Situational Awareness

CaPSS Canadian Peace, Stability and Security

CoPSS Continental Peace, Stability and Security

IPSS International Peace, Stability and Security



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For the year ended March 31

19. Segmented information (continued)

| (in thousands of dollars) | DTPS | CI | EPS | NSS |
|--|------------------|----------------|----------------|------------|
| Operating expense | | | | |
| Salary and employee benefits | 520,960 | 221,782 | 22,676 | 328 |
| Amortization | 7,430 | 0 | 0 | 0 |
| Professional and special services | 31,991 | 14,893 | 39,831 | 9 |
| Repair and maintenance | 48,595 | 14,677 | 247 | 0 |
| Transportation and communication | 296,365 | 21,788 | 923 | 8 |
| Materials and supplies | 8,041 | 25,793 | 1,243 | (40) |
| Expenses related to tangible assets | 8,549 | 4,410 | 235 | 1 |
| Other services | 97,335 | 4,340 | 12,351 | 26 |
| Other expenses | 80,508 | 16,400 | 67,468 | 57 |
| Accommodation | 11,016 | 8,769 | 219 | 2 |
| Utilities | 15,152 | 2,033 | 602 | 0 |
| Equipment and other rentals | 1,362 | 13,856 | 2,416 | 0 |
| Loss on disposals and write-offs and write-downs of assets | 0 | 0 | 0 | 0 |
| Interest on capital lease payments | 329 | 82 | 71 | 0 |
| Advertising, printing and related services | 357 | 296 | 25 | 0 |
| Bad debts | 146 | 66 | 6 | 1 |
| Total operating expenses | 1,128,136 | 349,185 | 148,313 | 392 |
| Transfer payments | | | | |
| Transfers to other countries and international organizations | 0 | 240 | 0 | 0 |
| Transfers to individuals | 0 | 0 | 3,014 | 0 |
| Transfers to other levels of government | 26 | 1,302 | 1,500 | 250 |
| Transfers to non-profit organizations | 3,649 | 0 | 0 | 0 |
| Total transfer payments | 3,675 | 1,542 | 4,514 | 250 |
| Total expenses | 1,131,811 | 350,727 | 152,827 | 642 |
| Revenues | | | | |
| Sale of goods and services | 113,684 | 229 | 41 | 0 |
| Gains on disposals of assets | 7 | 1 | 10 | 0 |
| Other | 1,271 | 7 | 1 | 0 |
| Interest and gains on foreign exchange | 14 | 10 | 0 | 0 |
| Revenues earned on behalf of Government | 0 | 0 | 0 | 0 |
| Total revenues | 114,976 | 247 | 52 | 0 |
| Net cost from continuing operations | 1,016,835 | 350,480 | 152,775 | 642 |

DTPS Defence Team Personnel Support
 CI Canadian Identity
 EPS Environment Protection and Stewardship
 NSS Non-Security Support



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

19. Segmented information (continued)

| (in thousands of dollars) | ISS | 2014 | 2013 (Restated note 20) |
|--|----------------|-------------------|----------------------------|
| Operating expense | | | |
| Salary and employee benefits | 587,259 | 9,658,529 | 10,712,642 |
| Amortization | 0 | 2,377,753 | 2,722,392 |
| Professional and special services | 65,183 | 1,658,285 | 1,909,063 |
| Repair and maintenance | 30,645 | 1,118,533 | 1,306,645 |
| Transportation and communication | 105,120 | 731,485 | 749,865 |
| Materials and supplies | 2,221 | 699,030 | 703,869 |
| Expenses related to tangible assets | 10,125 | 575,939 | 940,640 |
| Other services | 84,214 | 412,246 | 510,141 |
| Other expenses | (57,726) | 286,632 | 149,758 |
| Accommodation | 48,965 | 192,673 | 194,616 |
| Utilities | 291 | 172,848 | 160,889 |
| Equipment and other rentals | 1,811 | 159,740 | 180,333 |
| Loss on disposals and write-offs and write-downs of assets | 0 | 128,995 | 541,366 |
| Interest on capital lease payments | 0 | 26,058 | 29,249 |
| Advertising, printing and related services | 1,289 | 12,472 | 13,625 |
| Bad debts | 187 | 2,950 | (2,517) |
| Total operating expenses | 879,584 | 18,214,168 | 20,822,576 |
| Transfer payments | | | |
| Transfers to other countries and international organizations | (7,895) | 139,743 | 161,312 |
| Transfers to individuals | (541) | 9,187 | 9,385 |
| Transfers to other levels of government | 0 | 6,674 | 6,493 |
| Transfers to non-profit organizations | 0 | 3,649 | 4,203 |
| Total transfer payments | (8,436) | 159,253 | 181,393 |
| Total expenses | 871,148 | 18,373,421 | 21,003,969 |
| Revenues | | | |
| Sale of goods and services | 72,373 | 424,406 | 416,618 |
| Gains on disposals of assets | 2,692 | 22,232 | 36,070 |
| Other | 19,704 | 24,315 | 22,171 |
| Interest and gains on foreign exchange | 3,462 | 8,683 | 11,657 |
| Revenues earned on behalf of Government | (15,276) | (16,336) | (15,842) |
| Total revenues | 82,955 | 463,300 | 470,674 |
| Net cost from continuing operations | 788,193 | 17,910,121 | 20,533,295 |

ISS Internal Services



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the year ended March 31

20. Restatement of previous year's results

DND is undergoing a multi-year review of its business processes related to the recording and valuation of tangible assets and inventory. In 2013–14 this review identified capital assets and inventory transactions that should have been reported in previous fiscal years. The effects of the resulting retroactive adjustments are presented below:

| (in thousands of dollars) | 2013 As previously stated | Effect of changes | 2013 Restated |
|---|---------------------------------|----------------------|--------------------|
| Consolidated Statement of Financial Position | | | |
| Inventories (note 13) | 6,505,117 | (146,422) | 6,358,695 |
| Tangible capital assets (note 14) | 31,819,848 | (65,267) | 31,754,581 |
| Total non-financial assets | 38,934,987 | (211,689) | 38,723,298 |
| Departmental net financial position | 35,767,727 | (211,689) | 35,556,038 |
| Consolidated Statement of Operations and Departmental Net Financial Position | | | |
| Total expenses | 20,831,775 | 172,194 | 21,003,969 |
| Net cost from continuing operations | 20,361,101 | 172,194 | 20,533,295 |
| Net cost of operations after government funding and transfers | (370,680) | 189,898 | (180,782) |
| Departmental net financial position — beginning of year | 35,397,047 | (21,791) | 35,375,256 |
| Departmental net financial position — end of year | 35,767,727 | (211,689) | 35,556,038 |
| Consolidated Statement of Change in Departmental Net Debt | | | |
| Net cost of operations after government funding and transfers | (370,680) | 189,898 | (180,782) |
| Amortization of tangible capital assets | (2,709,530) | (12,862) | (2,722,392) |
| Adjustments of tangible capital assets | 14,784 | (30,614) | (15,830) |
| Change due to inventories | 286,313 | (146,422) | 139,891 |
| Consolidated Statement of Cash Flows | | | |
| Net cost of operations before government funding and transfers | 20,361,101 | 189,898 | 20,550,999 |
| Amortization of tangible capital assets | (2,709,530) | (12,862) | (2,722,392) |
| Adjustments of tangible capital assets | 14,784 | (30,614) | (15,830) |
| Increase in inventories | 286,313 | (146,422) | 139,891 |

21. Comparative Information

Comparative figures have been reclassified to conform to the current year's presentation.



ANNEX TO THE STATEMENT OF MANAGEMENT RESPONSIBILITY INCLUDING INTERNAL CONTROL OVER FINANCIAL REPORTING OF THE DEPARTMENT OF NATIONAL DEFENCE FOR FISCAL YEAR 2013–2014 (UNAUDITED)

1. Introduction

This document provides summary information on the measures taken by the DND to maintain an effective system of ICFR, including information on internal control management and assessment results and related action plans.

Detailed information on DND's authority, mandate and program activities can be found in Note 1 to these financial statements, as well as in the *Departmental Performance Report* and the *Report on Plans and Priorities*.

2. DND's System of Internal Control over Financial Reporting

2.1 Internal Control Management

DND has a well-established governance and accountability structure to support departmental assessment efforts and oversight of its system of internal control. Its control environment includes a series of measures and tools to enable its staff to effectively manage risks through raising awareness, providing appropriate knowledge, as well as developing skill sets. This control environment sets the tone for the Department, and is the foundation for its ICFR. An ICFR framework document signed by the DM is in place. Further, the Department has an internal control management framework in place which includes:

- Organizational accountability structures as they relate to internal control management to support sound financial management including roles and responsibilities for senior managers in their areas of responsibility;

- A Defence Ethics Program which is a comprehensive values-based ethics program put in place to meet the needs of DND and the CAF, at both the individual and the organizational levels;
- A comprehensive Fraud Risk Management Strategy that protects DND's resources from fraud, waste and abuse through a prevention and detection framework;
- An annually updated Corporate Risk Profile;
- On-going communication and training on statutory requirements, policies, and procedures for sound financial management and control; and
- Regular updates, at least semi-annually, on internal control assessments and action plans provided to departmental senior management, the departmental Director General Policy on Internal Control (PIC) Governance Committee, the Departmental Audit Committee (DAC) and to the DM. The DAC provides advice to the DM on the adequacy and functioning of the department's risk management, control and governance frameworks and processes.

2.2 Service arrangements relevant to financial statements

DND relies on other organizations for the processing of certain transactions that are recorded in its financial statements, and relies on these service providers to ensure an adequate system of ICFR is maintained over services provided to the Department. These include the following:



ANNEX TO THE STATEMENT OF MANAGEMENT RESPONSIBILITY INCLUDING INTERNAL CONTROL OVER FINANCIAL REPORTING OF THE DEPARTMENT OF NATIONAL DEFENCE FOR FISCAL YEAR 2013–2014 (UNAUDITED)

Common Arrangements:

- Public Works and Government Services Canada (PWGSC) centrally administers the payments of salaries, and beginning in 2013–14 under the *Consolidation of Pay Services Project*, is gradually transferring pay administration services for all DND civilian public servants to the Public Service Pay Centre (PSPC). PWGSC also centrally administers the procurement of goods and services, as per DND's Delegation of Authorities, and provides accommodation services;
- Treasury Board Secretariat (TBS) provides the Department certain services without charge, and also with information used to calculate various accruals and allowances, such as the accrued severance liability;
- The Department of Justice (DOJ) provides legal services to DND, as well as information for establishing the contingent liability note to the financial statements and for inclusion in the public accounts; and
- Shared Services Canada manages Information Technology General Controls (ITGCs) in the areas of email, data centre and network services.

Specific Arrangements:

- Defence Construction Canada (DCC) provides contracting, construction contract management and related infrastructure services to DND in accordance with the Memorandum of Understanding between the two organizations and as per DND's Delegation of Authorities;
- Brookfield Global Relocation Services administers DND moves under the CAF Integrated Relocation Program, which represents TBS' approved policy on relocation; and
- The Office of the Superintendent of Financial Institutions (OSFI) provides the Department with the accrued severance liability amount for the CAF.

3. DND's assessment results during fiscal year 2013–14

In 2013-2014, DND continued to make significant progress in the development, evaluation and remediation of Financial Control Frameworks (FCFs) in compliance with the Treasury Board of Canada *Policy on Internal Control* (PIC) for the majority of the DND's business processes. The Department has completed the evaluation of design effectiveness for most of its high risk processes, and has set up working groups to remediate identified weaknesses. In addition, work on Operating Effectiveness Testing and Ongoing Monitoring commenced during the year as planned. Details of assessments and results for 2013–14 are provided in the paragraphs that follow and in Table 1 of this annex.

3.1 Design effectiveness of key controls

The Department established eight internal control remediation working groups with representatives from across DND to resolve previously identified internal control gaps. The remediation working groups developed action plans for Capital Equipment and Real Property Assets, Material Acquisition and Support (MA&S) processes, Procurement, Payables and Payments, Acquisition Cards, Revenue, Receivables & Receipts, Civilian Payroll, Regular Force and Reserve Payroll business processes.

3.2 Operating effectiveness of key controls

DND began operating effectiveness testing for Prepaid Foreign Military Sales (FMS) and the Revenue, Receivables and Receipts business processes. Testing was completed for key controls within the FMS prepaid expense process, and remediation of identified gaps will be addressed in 2014–15. Testing for the Revenue, Receivables and Receipts process is scheduled for completion in September 2014.

As part of this exercise, an operating effectiveness testing approach and reporting templates were developed to be used going forward for operating effectiveness testing of key controls in other financial statement areas at DND.



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3.3 On-going monitoring of key controls

In 2013–14, the Department commenced planned on-going monitoring of Entity-Level Controls (ELCs) and ITGCs. DND developed a risk-based approach to ongoing monitoring, and using this as a basis, ongoing monitoring of both areas commenced on selected controls.

Though on-going monitoring of these areas has commenced, some remediation resulting from the evaluation of design and operating effectiveness still remain, and will be monitored and reported on to ensure compliance with PIC.

4. DND’s action plan

4.1 Progress during fiscal year 2013–14

In 2013–14, DND continued to make significant progress towards the implementation of an effective system of ICFR for the majority of the Department’s financial business processes. Table 1 below summarizes a third party assessment of DND’s progress as at 31 March 2014.

Table 1 — DND’s Progress against its 2012–13 Action Plan

| Element in 2012–13 Action Plan | Status |
|---|---|
| Entity Level Controls (ELCs) — Operating effectiveness testing and remediation | Met During 2013–14, DND started ongoing monitoring of ELCs based on an approved risk-based monitoring plan. Year 1 testing is expected to be completed by September 2014. Updates to DND’s ELC framework were also made based on additional evidence gathered during testing. |
| Information Technology General Controls (ITGCs) — Operating effectiveness testing and remediation | Met DND developed a 3 year risk-based approach to the ongoing assessment and monitoring of ITGCs. The yearly approach involves performing an annual assessment to determine which of the ITGCs included in the established DND specific Control Objective for Information and Related Technology (COBIT) controls framework are key to supporting the relevant business process controls, and testing those controls. Based on this approach, DND completed Year 1 of the ongoing monitoring for controls related to PeopleSoft HRMS. Results indicate that while a number of the previously identified high risk gaps have been remediated, some still remain, and additional low risk gaps have been identified. The Department also commenced Year 1 of ongoing monitoring for controls related to the Defence Resource Management Information System (DRMIS (SAP)). These controls are currently being tested with an expectation of completion of Year 1 testing by end of September 2014. |



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Table 1 — DND’s Progress against its 2012–13 Action Plan (continued)

| Element in 2012–13 Action Plan | Status |
|--|---|
| Financial Reporting and Financial Statement Preparation — Design effectiveness testing and remediation | <p>Substantially met</p> <p>Ad hoc remediation meetings were held in 2013–14 to address previously identified control deficiencies, and a remediation action plan was used to document, track and follow-up on commitments made and agreed to by departmental subject matter experts.</p> <p>A report on the results of remediation efforts, including a description of progress made during the year and an updated remediation action plan was prepared and will be used going forward to address the remaining three gaps that have not yet been fully remediated.</p> <p>The update of process documentation was also initiated to account for recent changes to the process, including modifications to the financial statements as per Treasury Board Accounting Standards.</p> |
| Revenue and Receivables — Design effectiveness testing and remediation | <p>Met</p> <p>In 2013–14, the Revenue and Receivables Working Group, which was formed in 2012–13, completed its work by finalizing its remediation action plan to address outstanding design effectiveness gaps. The implementation of remediation activities was completed for all areas with the exception of some of those pertaining to DRMIS.</p> <p>During the year, DND also commenced operating effectiveness testing of the revenue and receivables FCF. Testing is scheduled for completion in September 2014 after which remediation will begin for identified operating effectiveness gaps, if any. The outstanding DRMIS design effectiveness gaps will also continue to be addressed and monitored as part of this remediation effort.</p> |
| Prepaid Expenses — Operating effectiveness testing | <p>Met</p> <p>In 2013–14, the FCF designed for the FMS prepaid process was reviewed and updated to reflect changes since documentation and design effectiveness testing was completed.</p> <p>In addition, operating effectiveness testing was performed on key controls within the FMS prepaid expense process, including the payment process and the semi-annual prepaid process for all FMS cases except Cooperative Logistics Supply Support Arrangement (CLSSA, commonly referred to as COLOG).</p> <p>Following the testing, a report was developed which included the following recommendations: documentation and implementation of formal approval processes; creation and use of standardized tools for review; and consistent and identifiable signatures and financial coding to be included with supporting documentation.</p> |



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Table 1 — DND's Progress against its 2012–13 Action Plan (continued)

| Element in 2012–13 Action Plan | Status |
|--|---|
| <p>Procurement to payment — Design effectiveness testing and remediation</p> | <p>Met</p> <p>During 2013–14, remediation activities continued for ten processes previously evaluated for design effectiveness. A remediation action plan was developed to document the commitments made and agreed to by the members of the Procure to Pay Remediation Working Group. Remediation items were further progressed and in some cases, completed and closed, such as the implementation of a standardized Post Payment Verification process and controls across DND.</p> <p>In addition, an Acquisition Card Remediation Working Group was established to identify remediation measures for the control deficiencies identified in the evaluation of acquisition card design effectiveness. A remediation action plan was developed to document the commitments made and agreed to by the working group members.</p> <p>DND also commenced the development of FCFs for additional sub-processes within the Procurement to Payment business cycle, including Grants and Contributions, Vessel Cards and Procurement within the Financial Accounting (FI) module of DRMIS. An evaluation of design effectiveness was completed during the year for the grants and contributions processes and FCFs.</p> <p>Additionally, meetings were held with subject matter experts to remediate the previously identified design effectiveness gaps in the payables-at-year-end (PAYE) and contract holdback business processes. Remediation activities were completed for the contract holdback process, and remediation action plans were developed and agreed upon by subject matter experts for the PAYE process.</p> |
| <p>Civilian Payroll and Payroll Liabilities — Design effectiveness testing and remediation</p> | <p>Met</p> <p>During 2013–14, DND updated the civilian payroll FCF documentation to consider the impact of the PWGSC Consolidation of Pay Services Project. Civilian Payroll Remediation Working Group sessions were also finalized in 2013–14 and a remediation action plan was developed to document the commitments made and agreed to by the working group members. With the integration of the PSPC at PWGSC and the finalization and communication of its Quality Assurance (QA) Program to departments, the remediation of many civilian payroll control deficiencies was expedited and/or remediated through the implementation of pay consolidation. Due to PWGSC's timeline for submission of the QA Program to departments, DND was not able to fully execute the implementation of the Department's portion of the QA Program by 31 March 2014.</p> |



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Table 1 — DND's Progress against its 2012–13 Action Plan (continued)

| Element in 2012–13 Action Plan | Status |
|--|--|
| <p>Military Regular Force Payroll — Design effectiveness and remediation</p> | <p>Met</p> <p>A Military Regular Force Payroll Remediation Working Group was established in 2013–14 to identify remediation measures to the control deficiencies identified in the evaluation of design effectiveness testing. A remediation action plan was developed to document the commitments made and agreed to by the working group members.</p> <p>Remediation efforts considered the Pay Administration Control Framework Tool (PA-CF) developed by the Office of the Comptroller General (OCG) to the extent that it was applicable as it is based on a civilian payroll environment. Military Personnel Management Capability Transformation (MPMCT) project representatives actively participated in the remediation working group to ensure remediation measures are considered in the implementation of the new military payroll process. The Military Regular Force payroll FCF documentation was also presented to the MPMCT Project Steering Committee.</p> |
| <p>Military Reserve Force Payroll — Design effectiveness and remediation</p> | <p>Met</p> <p>Design effectiveness testing for military reserve force payroll was finalized in 2013–14. A Reserve Force Payroll Remediation Working Group was also established and finalized in 2013–14 to identify remediation measures to the control deficiencies identified in the evaluation of design effectiveness testing. A remediation action plan was developed to document the commitments made and agreed to by the working group members.</p> <p>Remediation efforts considered the PA-CF developed by the OCG to the extent that it was applicable as it is based on a civilian payroll environment. MPMCT project representatives actively participated in the remediation working group to ensure that remediation measures are considered in the implementation of the new military payroll process. The Military Reserve Force payroll FCF documentation was also presented to the MPMCT Project Steering Committee.</p> |
| <p>Inventories — Design effectiveness and remediation</p> | <p>Met</p> <p>During 2013–14, documentation and design effectiveness testing was completed on outstanding processes relative to inventory valuation and reporting. In addition to this, the MA&S Remediation Working Group reviewed all control deficiencies identified through the MA&S design effectiveness testing, agreed on a remediation action plan including remediation ownership and completion deadlines. A draft remediation report outlining the remediation action plan that had been committed to by members of the working group was issued.</p> |



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Table 1 — DND's Progress against its 2012–13 Action Plan (continued)

| Element in 2012–13 Action Plan | Status |
|---|--|
| Capital equipment assets — Design effectiveness and remediation | <p>Met</p> <p>During 2013–14, the Tangible Capital Asset Remediation Working Group was established and tasked with reviewing all control deficiencies identified through the Capital Equipment Assets and Real Property Assets test of design effectiveness. A remediation action plan, including remediation ownership and completion deadlines, was agreed upon. Through a series of bi-weekly working sessions, the working group reviewed all control deficiencies. A draft report outlining the remediation action plans that were committed to by the working group members was issued. In addition, work on the planning of remediation efforts related to Asset Pooled Items (APIs) commenced during the year.</p> |
| Real property assets — Design effectiveness and remediation | <p>Met</p> <p>During 2013–14, updated FCF documentation and the test of design effectiveness of controls for Real Property Assets was completed. A report on the results of design effectiveness testing was then issued, and remediation efforts of the identified control deficiencies were incorporated into the Tangible Capital Asset Remediation Working Group Action Plan.</p> |
| Remediation liabilities — Design effectiveness and remediation | <p>Met</p> <p>A solution to manage Contaminated Sites and the associated Remediation Liabilities was implemented in DRMIS through the replacement of the EcoNet legacy system. As a result of this replacement, DND updated the contaminated sites FCF and significantly progressed the evaluation of design effectiveness of the revised business process. It was noted that the implementation of DRMIS solution had addressed several previously identified control deficiencies associated with EcoNet.</p> |



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4.2 Status and action plan for the next fiscal year and subsequent years

Building on progress to date, DND is positioned to complete the assessment of the majority of its system of ICFR by 2016–17. At that time, the Department will be applying its risk-based rotational on-going monitoring plan to reassess control performance across those control areas that have been fully assessed.

It is important to note that due to the size and complexities of DND's operations, full PIC implementation will only be achieved when the departmental business transformation and IT projects are completed. Highlights of these interdependencies are as follows:

Military Regular and Reserve Force Payroll: The MPMCT project for Regular Force and Reserve Force pay administration is planned for full implementation by 2018. Following this, all identified design effectiveness control deficiencies will be remediated and operating effectiveness testing and remediation will begin.

Civilian Payroll: The Government of Canada Consolidation of Pay Services Project led by PWGSC has a phased implementation approach which began in October 2013 with a planned completion date of December 2015. DND will begin operating effectiveness testing and remediation in a pay consolidation environment in 2014–15.

Inventory and Capital Equipment Assets: In addition to PIC remediation activities, there are various other projects and plans underway to improve inventory and capital asset management including reporting accuracy.

With the Supply Chain Integration (SCI) project (migration of data from the legacy supply system into DRMIS) being substantially completed, efforts are being focused on retiring the legacy system, including ensuring that data migration issues identified during the transition to DRMIS are resolved.

As part of its MA&S Transformation Plan, DND is undertaking cross-functional materiel management initiatives to improve processes, including reporting accuracy. For example, one of these initiatives, the Inventory Management Modernization and Rationalization Project (IMMRP) is a long-term project that will likely impact the remediation of inventory findings.

Due to many interdependencies and complexities in this area, the completion of these ICFR frameworks is at risk to be fully implemented by the 2016–17 timeline.

Real Property Assets: Implementation of the Infrastructure Environment Business Modernization (IEBM) Phase 2 will begin in 2015–16. Documentation of the financial control frameworks for the remainder of the sub-processes around Real Property Assets will commence shortly after the IEBM Phase 2 implementation.



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DND's action plan summarized below in Table 2 is based on current resources as well as the interdependencies described above. As such, it is impacted by changes to resource levels and project outcomes and will be reviewed annually.

Table 2 — Status and Action Plan for the Completion of Identified Control Areas

| Key Control Area | ASSESSMENT ELEMENTS | | |
|--|--|---|------------------------------|
| | Design effectiveness testing and remediation | Operating effectiveness testing and remediation | On-going monitoring rotation |
| Entity Level Controls (ELCs) | Completed | Completed | ✓ |
| IT General Controls | Completed | Completed | ✓ |
| Financial Reporting and Financial Close¹ | 2015–16 | 2016–17 | 2016–17 |
| Process Level Controls: | | | |
| Revenues and Receivables | Completed | 2014–15 | 2015–16 |
| Prepaid Expenses | Completed | 2014–15 | 2015–16 |
| Procurement to Payment | 2015–16 | 2016–17 | 2016–17 |
| Other Payables and Payments ² | 2015–16 | 2016–17 | 2016–17 |
| Civilian Payroll & Payroll Liabilities | Completed | 2015–16 | 2016–17 |
| Military Regular & Reserve Force Payroll | 2015–16 | 2017–18 | 2018–19 |
| Inventories | 2015–16 | 2016–17 | Future years |
| Capital Equipment Assets | 2015–16 | 2016–17 | Future years |
| Real Property Assets | 2015–16 | 2016–17 | Future years |
| Remediation Liabilities | 2014–15 | 2015–16 | 2016–17 |

¹ Building on work completed to date on financial reporting, DND has included *Financial Close* as a departmental process under PIC to properly align with the OCG's Common Financial Management Business Process (FM-BP) Initiative. Target dates have been amended accordingly to achieve design effectiveness and remediation of control deficiencies for both processes.

² Other Payables and Payments include unique procure to pay processes, such as Acquisition Cards, Contract Holdbacks, Departmental Travel Cards and payments originating from source systems that interface with DND's ERP system. Due to business transformation and rationalization activities, legacy source systems are expected to be retired and ICFR documentation and implementation of financial controls will progress with these transformation initiatives.



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