Financial Statements

YEAR ENDED 31 DECEMBER 1999

Bank of Canada
Financial reporting responsibility

The accompanying financial statements of the Bank of Canada have been prepared by management in accordance with accounting principles generally accepted in Canada and these principles have been consistently applied. The integrity and objectivity of the data in these financial statements are management's responsibility. Management is responsible for ensuring that all information in the annual report is consistent with the financial statements.

In support of its responsibility, management maintains financial and management control systems and practices to provide reasonable assurance that the financial information is reliable, that the assets are safeguarded, and that the operations are carried out effectively. The Bank has an internal audit department, whose functions include reviewing internal controls and their application on an ongoing basis.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control and exercises this responsibility through the Audit Committee of the Board. The Audit Committee reviews the Bank's annual financial statements and recommends their approval by the Board of Directors. The Audit Committee meets with management, the internal auditor, and the Bank's external auditors appointed by Order-in-Council.

These financial statements have been audited by the Bank's external auditors, Caron Bélanger Ernst & Young and Raymond Chabot Grant Thornton, and their report is presented herein.

G.G. Thiessen, Governor

L.T. Requard, Corporate Secretary

Ottawa, Canada

AUDITORS OF THE BANK OF CANADA
VÉRIFICATEURS DE LA BANQUE DU CANADA

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CARON BÉLANGER ERNST & YOUNG | RAYMOND CHABOT GRANT THORNTON

AUDITORS' REPORT

To the Minister of Finance, registered shareholder of the Bank of Canada

We have audited the balance sheet of the Bank of Canada as at 31 December 1999 and the statement of revenue and expense for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 1999 and the results of its operations and cash flow for the year then ended in accordance with generally accepted accounting principles.

Caron Bélanger Ernst & Young
Chartered Accountants

Raymond Chabot Grant Thornton
Chartered Accountants

Ottawa, Canada
21 January 2000

Bank of Canada
Statement of revenue and expense

Year ended 31 December 1999

	1999	1998
	Millions of dollars	
REVENUE		
Revenue from investments	**1,910.8**	1,799.4
EXPENSE by function (notes 1 and 4)		
Monetary policy	**39.0**	40.7
Currency	**72.7**	57.5
Central banking services	**33.0**	30.7
	144.7	128.9
Retail debt services – expenses	**73.9**	65.5
Retail debt services – recoveries	**(73.9)**	(65.5)
Other revenue – net	**–**	(8.3)
	144.7	120.6
NET REVENUE PAID TO RECEIVER GENERAL FOR CANADA	**1,766.1**	1,678.8

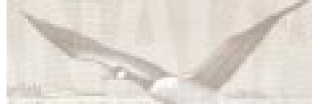
(See accompanying notes to the financial statements.)

Bank of Canada
Balance sheet

As at 31 December 1999

ASSETS	**1999**	**1998**
	Millions of dollars	
Deposits in foreign currencies		
U.S. dollars	**605.6**	321.1
Other currencies	**4.4**	6.2
	610.0	327.3
Advances to members of the Canadian Payments Association	**560.7**	655.7
Investments (note 3)		
Treasury bills of Canada	**12,020.6**	12,115.5
Other securities issued or guaranteed by Canada maturing within three years	**7,515.1**	6,302.2
Other securities issued or guaranteed by Canada not maturing within three years	**12,975.7**	10,880.1
Other investments	**5,130.9**	4,455.7
	37,642.3	33,753.5
Bank premises (note 4)	**175.2**	188.0
Other assets		
Securities purchased under resale agreements	**3,669.6**	–
All other assets (note 5)	**405.5**	436.4
	4,075.1	436.4
	43,063.3	35,360.9

(See accompanying notes to the financial statements.)



LIABILITIES	1999	1998
	Millions of dollars	
Capital paid up (note 6)	**5.0**	5.0
Rest fund (note 7)	**25.0**	25.0
Bank notes in circulation	**40,142.6**	32,637.5
Deposits		
Government of Canada	**11.8**	10.6
Banks	**1,827.8**	578.7
Other members of the Canadian Payments Association	**119.5**	73.5
Other deposits	**428.5**	243.7
	2,387.6	906.5
Liabilities in foreign currencies		
Government of Canada	**454.5**	162.0
Other liabilities		
Securities sold under repurchase agreements	**–**	1,551.9
All other liabilities	**48.6**	73.0
	48.6	1,624.9
	43,063.3	35,360.9

Governor, G.G. Thiessen

Chief Accountant, F.J. Mahoney

Chairman, Audit Committee, W. Dubowec, FCA

Lead Director, H.H. MacKay, QC

(See accompanying notes to the financial statements.)

Bank of Canada
Notes to the financial statements

Year ended 31 December 1999

1. Bank functions

The Bank of Canada's primary responsibilities are set out in the Bank of Canada Act and can be grouped into four broad functions, which are described below. Net operating expenses in the *Statement of revenue and expense* are reported on the basis of these four corporate functions. Certain comparative figures have been reclassified to conform with the financial statement presentation adopted in the current year.

Monetary policy

The Bank's most important responsibility is monetary policy. Monetary policy is concerned with managing the rate of monetary expansion in a way that is consistent with preserving the value of money.

Currency

The Bank is responsible for issuing bank notes in Canada. This responsibility involves note design (including anti-counterfeiting features), as well as the printing and distribution of bank notes and their eventual replacement.

Central banking services

The Bank carries out a variety of activities that regulate and support Canada's principal systems for clearing and settling payments and other financial transactions. The Bank also provides a number of central banking services and advice to the federal government, financial institutions, and the general public. As fiscal agent, the Bank advises the federal government on matters relating to the public debt and is responsible for issuing market debt, maintaining bondholder records, and making payments on behalf of the government for interest and debt redemption.

Retail debt services

The Bank provides systems and operational support services to the Canada Investment and Savings agency (CI&S) in support of the federal government's retail debt program and is responsible for issuing debt, maintaining bondholder records, and making payments on behalf of the federal government for interest and debt redemption. The Bank recovers the cost of retail debt operations on a full-cost basis.

2. Significant accounting policies

The financial statements of the Bank are in accordance with generally accepted accounting principles and conform to the disclosure and accounting requirements of the Bank of Canada Act and the Bank's by-laws. As all material changes in financial position are evident from the financial statements, a separate statement of cash flow has not been prepared as it would not provide any additional useful information. The significant accounting policies of the Bank are:

a) Revenues and expenses

Revenues and expenses are accounted for on the accrual basis.

b) Translation of foreign currencies

Assets and liabilities in foreign currencies are translated to Canadian dollars at the rates of exchange prevailing at the year-end. Foreign currency assets held under short-term foreign currency swap arrangements with the Exchange Fund Account of the Government of Canada, as described in note 9(a), are converted to Canadian dollars at the contracted rates. Gains and losses from translation of, and transactions in, foreign currencies are included in revenue.

c) Advances

Advances to members of the Canadian Payments Association are liquidity loans which are fully collateralized and generally overnight in duration. The Bank charges interest on advances under the Large Value Transfer System (LVTS) at the Bank Rate. For advances under the Automated Clearing Settlement System, the Bank charges the Bank Rate plus a margin, which was 150 basis points at 31 December 1999 (Bank Rate prior to introduction of the LVTS on 4 February 1999).

d) Investments

Investments, consisting mainly of Government of Canada treasury bills and bonds, are recorded at cost and are adjusted for amortization of purchase discounts and premiums. The amortization, as well as gains and losses on disposition, is included in revenue.

e) Bank premises

Bank premises, consisting of land, buildings, computer hardware / software, and other equipment, are recorded at cost less accumulated depreciation. Computer software is capitalized only when its cost exceeds $2 million. Depreciation is calculated using the straight-line method and is applied over the estimated useful lives of the assets, as shown below.

Buildings	25 to 40 years
Computer hardware / software	3 to 7 years
Other equipment	5 to 15 years

f) Special purchase and resale agreements (SPRAs)

SPRAs are repo-type transactions in which the Bank of Canada offers to purchase Government of Canada securities from designated counterparties with an agreement to sell them back at a predetermined price the next business day. Within the operating band for the overnight interest rate, the Bank is prepared to enter into SPRAs at the policy target rate (i.e., the midpoint of the band) if overnight funds are generally trading above the indicated target level. SPRAs are transacted with primary dealers, a subgroup of government securities distributors that have reached a threshold level of activity in the Government of Canada debt markets. The balance sheet category *Securities purchased under resale agreements* represents the value receivable by the Bank upon resale of the securities. As such, this amount includes the purchase of treasury bills and bonds, the purchase of accrued interest on bonds, and the interest earned by the Bank over the duration of the SPRAs. The treasury bills and bonds purchased under resale agreements are not recorded as investment assets.

In the course of 1999, the Bank adopted the method of accounting for SPRAs described above. Previously, securities acquired under SPRAs were included in the Bank's investment holdings. There were no SPRAs outstanding at 31 December 1998. Thus, no restatements have been required for the comparative year.

g) Deposits

The liabilities within this category are Canadian dollar demand deposits. The Bank did not pay interest on deposits for *Banks* and *Other members of the Canadian Payments Association* prior to the introduction of the LVTS on 4 February 1999. For members of the Canadian Payments Association, the Bank pays interest on positive balances associated with the Large Value Transfer System (LVTS) at the lower end of the operating band for the overnight interest rate, and on positive balances related to the Automated Clearing Settlement System at the lower end of the operating band for the overnight interest rate less a margin, which was 150 basis points at 31 December 1999. On Special Deposit Accounts, which serve as collateral for LVTS participants, the Bank pays interest at the published overnight rate less a margin, which was 6.25 basis points at 31 December 1999.

h) Sale and repurchase agreements (SRAs)

SRAs are reverse repo-type transactions in which the Bank of Canada offers to sell Government of Canada securities to designated counterparties with an agreement to buy them back at a predetermined price the next business day. Within the operating band for the overnight interest rate, the Bank is prepared to enter into SRAs at the policy target rate (i.e., the midpoint of the band) if overnight funds are generally trading below the indicated target level. SRAs are transacted with primary dealers, a subgroup of government securities distributors that have reached a threshold level of activity in the Government of Canada debt markets.

The balance sheet category *Securities sold under repurchase agreements* represents the value payable by the Bank upon repurchase of the securities. As such, this amount includes the sale of treasury bills and bonds, the sale of accrued interest on bonds, and the interest owed by the Bank over the duration of the SRAs. The treasury bills and bonds sold under repurchase agreements continue to be recorded as investment assets.

In the course of 1999, the Bank adopted the method of accounting for SRAs described above. Previously, securities sold under SRAs were excluded from the Bank's investment holdings. SRA repurchase commitments, valued for settlement on 4 January 1999 and totalling $1,552.5 million, were outstanding at 31 December 1998. Thus, it has been necessary to make the following restatements for the comparative year. The Bank's assets under *Investments – Treasury bills of Canada* have been increased by the value of the securities sold under SRAs ($1,551.7 million). The Bank's liabilities in the new category *Other liabilities – Securities sold under repurchase agreements* have been increased by the value of the securities sold under SRAs and the one day of interest owed by the Bank for 1998 ($1,551.9 million). Finally, the category *All other liabilities* has been reduced by the one day of interest payable for 1998 ($0.2 million) that is now reflected in *Securities sold under repurchase agreements*.

i) Insurance

The Bank does not insure against direct risks of loss to the Bank, except for potential liabilities to third parties and where there are legal or contractual obligations to carry insurance. Any costs arising from these risks are recorded in the accounts at the time they can be reasonably estimated.

3. Investments

This category includes Government of Canada treasury bills and bonds as well as other investments, which are held under short-term foreign currency swap arrangements with the Exchange Fund Account of the Government of Canada as described in note 9(a).

The Bank typically holds its investments in treasury bills and bonds until maturity. The amortized book values of these investments approximate their par values. At the year-end, the average yield on the Bank's holdings of treasury bills, which average three months to maturity was 4.9 per cent (5.0 per cent in 1998), while the average yield for bonds maturing within three years was 6.5 per cent (6.6 per cent in 1998), and for those maturing in over three years was 6.6 per cent (6.9 per cent in 1998).

4. Bank premises

	1999			**1998**		
	Millions of dollars					
	Cost	Accumulated depreciation	Net book value	Cost	Accumulated depreciation	Net book value
Land and buildings	**168.0**	**68.5**	**99.5**	168.0	65.1	102.9
Computer hardware/ software	**62.0**	**28.8**	**33.2**	61.6	24.6	37.0
Other equipment	**137.1**	**94.6**	**42.5**	136.5	88.4	48.1
	367.1	**191.9**	**175.2**	366.1	178.1	188.0

Total depreciation on Bank buildings, computer hardware and software, and other equipment was $28.3 million for 1999 ($23.7 million in 1998).

5. All other assets

This category includes accrued interest on investments of $325.6 million ($352.1 million in 1998).

6. Capital paid up

The authorized capital of the Bank is $5.0 million divided into 100,000 shares with a par value of $50 each. The shares are fully paid and, in accordance with the Bank of Canada Act, have been issued to the Minister of Finance, who is holding them on behalf of the Government of Canada.

7. Rest fund

The rest fund was established in accordance with the Bank of Canada Act and represents the general reserve of the Bank. The rest fund was accumulated out of net revenue until it reached the stipulated maximum amount of $25.0 million in 1955.

8. Pension plan

The Bank sponsors a defined-benefit pension plan for its employees, which is registered under the Pension Benefits Standards Act. The plan provides pension benefits based on length of service and rates of pay.

Actuarial valuations of the pension plan are made periodically by an independent actuary using the projected benefit method prorated on service. Market-related values are used to value pension plan assets. Based on the latest actuarial valuation as at 1 January 1999, the estimated present value of the accrued pension benefits as at 31 December 1999 was $478.2 million ($449.6 million in 1998), and the estimated market-related value of the pension plan assets was $600.5 million ($565.5 million in 1998).

Pension expense for 1999 was in a credit position of $4.6 million ($4.3 million in 1998). These amounts comprise the actuarially computed cost of pension benefits in respect of current year service and the amortization of past service costs and experience gains and losses. Amortization is calculated on a straight-line basis over the expected average remaining service life of the plan members, currently 12 years.

9. Commitments

a) Foreign currency contracts

In the ordinary course of business, the Bank enters into commitments involving the purchase and sale of foreign currencies. In particular, the Bank enters into short-term foreign currency swap arrangements with the Exchange Fund Account (EFA) of the Government of Canada as part of its cash-management operations within the Canadian banking system. These transactions, which are made with the concurrence of the Minister of Finance under a standing authority, involve the temporary acquisition by the Bank of foreign currency investments from the EFA. These investments are paid for in Canadian dollars at the prevailing exchange rate with a commitment to reverse the transaction at the same rate of exchange at a future date. The fair values of these investments are not materially different from their book values. At the year-end, the average yield for these investments was 5.5 per cent (6.0 per cent in 1998).

As well, the Bank of Canada is a participant in two foreign currency swap facilities with foreign central banks. The first, amounting to US$2 billion, is with the U.S. Federal Reserve. The second, amounting to Can$1 billion, is with the Banco de México. There were no drawings under either facility in 1999 or 1998.

All commitments outstanding at 31 December are settled in the subsequent year. A summary of these outstanding commitments follows.

		1999	1998
		Millions of dollars	
Foreign currency contracts	– purchases	**117.6**	95.6
	– sales	**5,299.9**	4,644.3

As at 31 December 1999, outstanding foreign currency contracts included sale commitments of $5,182.4 million ($4,548.7 million in 1998) under swap arrangements with the EFA.

b) Investment contracts

In the ordinary course of business, the Bank enters into commitments involving the purchase and sale of securities. All commitments outstanding at 31 December are settled in the subsequent year. A summary of these outstanding commitments follows.

		1999	1998
		Millions of dollars	
Investment contracts	– purchases	**–**	1,552.5
	– sales	**3,675.0**	–

As at 31 December 1999, there were no outstanding purchase investment contracts ($1,552.5 million at an interest rate of 4.75 per cent at the end of 1998 under Sale and Repurchase Agreements). Outstanding sale investment contracts of $3,675.0 million, at an interest rate of 4.75 per cent under Special Purchase and Resale Agreements, were settled by 13 January 2000 (nil at the end of 1998).

10. Year 2000

The year-2000 computer issue arose chiefly because many date-sensitive automated systems had not been designed to recognize correctly the year 2000. This represented a significant challenge for all organizations. If not addressed properly, the year-2000 issue could have had an impact on operations and financial reporting, ranging from minor errors to the failures of critical systems. The year 2000 arrived without incident for the Bank. However, as is the case generally, it is not yet possible to conclude definitively that all aspects of the year-2000 issue affecting the Bank, including those related to the efforts of clients, suppliers, or other third parties, have been fully resolved.