



# Realpool Investment Fund

DECEMBER 2017

**British Columbia Investment Management Corporation  
Realpool Investment Fund**

**MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING**

British Columbia Investment Management Corporation [BCI] manages the Realpool Investment Fund [Fund] on behalf of governing fiduciaries such as pension fund trustees and other public sector clients.

The 2017 financial statements of the Fund have been prepared by management of BCI and approved by the Chief Investment Officer/Chief Executive Officer. The financial statements have been prepared in accordance with International Financial Reporting Standards. The significant accounting policies used in the preparation of these statements are disclosed in note 3 to the financial statements. The statements include certain amounts that are based on management's judgment and best estimates.

BCI's Board has established an Audit Committee. The Committee's mandate includes making recommendations on the appointment of the external auditor for the Realpool Investment Fund, reviewing the external audit plan, reviewing BCI's Service Organization Controls Report for the Investment System of British Columbia Investment Management Corporation, and reviewing the annual audited financial statements of the Realpool Investment Fund. The Committee reviews the recommendations of the internal and external auditors with respect to internal controls and the responses of management to those recommendations, and also meets with management and the internal and external auditors to review annual audit plans.

BCI maintains systems of internal control and supporting processes to provide reasonable assurance that assets are safeguarded; that transactions are appropriately authorized and recorded; and that there are no material misstatements in the financial statements. BCI's internal control framework includes: a strong corporate governance structure; a code of conduct that includes conflict of interest guidelines; an organizational structure that provides for appropriate segregation of duties and accountability for performance; an enterprise-wide risk management framework that identifies, monitors and reports on key risks; and Board-approved Pooled Investment Portfolio Policies and client-approved investment mandates. BCI's system of internal control is supported by external auditors who review and evaluate internal controls and report directly to the Audit Committee.

The Fund's external auditors, Ernst & Young LLP ["EY"], have full and unrestricted access to the Audit Committee and BCI management. EY discusses with management and the Committee the results of their audit of the Fund's financial statements and related findings with respect to such audit. The Fund is audited by EY in accordance with Canadian generally accepted auditing standards. EY has performed such tests and other procedures as they considered necessary to express an opinion on the Fund's financial statements.

**[S] Gordon J. Fyfe**

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Gordon J. Fyfe  
Chief Executive Officer/Chief Investment Officer

**[S] Lawrence E. Davis**

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Lawrence E. Davis  
Senior Vice President, Finance

# Independent auditors' report

To the Unitholders of  
**Realpool Investment Fund**

We have audited the accompanying financial statements of **Realpool Investment Fund**, which comprise the statement of financial position as at December 31, 2017, and the statements of comprehensive income, changes in net assets attributable to holders of redeemable units and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

## Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

## Auditors' responsibility

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

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

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

## Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of **Realpool Investment Fund** as at December 31, 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Vancouver, Canada  
April 5, 2018

*Ernst & Young LLP*

Chartered Professional Accountants



BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND

**Statement of Financial Position**

(all amounts in thousands except number of units)

	Note	December 31, 2017	December 31, 2016
<b>Assets</b>			
Cash and cash equivalents		\$ 177,788	\$ 81,429
Receivable from issue of redeemable units		95,000	-
Dividends receivable		-	114
Interest receivable		701	1,092
Investments at fair value through profit or loss	4, 8	15,501,404	15,251,997
		<u>15,774,893</u>	<u>15,334,632</u>
<b>Liabilities</b>			
Payable for redemption of units		-	93,830
External management fees payable		40	-
BCI cost recoveries payable	5	8,431	1,310
Other accounts payable		<u>515</u>	<u>1,012</u>
Total liabilities excluding net assets attributable to holders of redeemable units		<u>8,986</u>	<u>96,152</u>
<b>Net assets attributable to holders of redeemable units</b>		<u><b>\$ 15,765,907</b></u>	<u><b>\$ 15,238,480</b></u>
<i>Number of redeemable units outstanding</i>	6	<i>1,627.092</i>	<i>1,652.774</i>
<b>Net assets attributable to holders of redeemable units per unit</b>		<u><b>\$ 9,690</b></u>	<u><b>\$ 9,220</b></u>

**Statement of Comprehensive Income**

(all amounts in thousands)

	Note	Year Ended December 31, 2017	Year Ended December 31, 2016
<b>Revenue:</b>			
Interest income		\$ 83,894	\$ 86,293
Dividend income		-	1,367
Income from money market funds		1,434	674
Change in fair value of investments:	8		
Net realized gain		286,519	1,682,211
Net change in unrealized appreciation (depreciation)		<u>409,871</u>	<u>(973,862)</u>
Total revenue		<u>781,718</u>	<u>796,683</u>
<b>Expenses:</b>			
BCI cost recoveries	5	15,268	12,673
Other management fees		666	320
Administrative and professional fees		3,242	2,220
Pursuit cost		<u>115</u>	<u>325</u>
Total operating expenses		<u>19,291</u>	<u>15,538</u>
Increase in net assets attributable to holders of redeemable units from operations excluding distributions		<u>762,427</u>	<u>781,145</u>
Distributions to holders of redeemable units		<u>(487,721)</u>	<u>(1,794,164)</u>
<b>Increase (decrease) in net assets attributable to holders of redeemable units</b>		<u><b>\$ 274,706</b></u>	<u><b>\$ (1,013,019)</b></u>

[S] Gordon J. Fyfe

Gordon J. Fyfe  
Chief Executive Officer  
Chief Investment Officer

See accompanying notes to the financial statements.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND

**Statement of Changes in Net Assets Attributable to Holders of Redeemable Units**  
(all amounts in thousands)

	Year Ended December 31, 2017	Year Ended December 31, 2016
Balance, beginning of year	\$ 15,238,480	\$ 14,921,065
Increase (decrease) in net assets attributable to holders of redeemable units	274,706	(1,013,019)
Redeemable unit transactions:		
Proceeds from units issued	155,000	-
Reinvestment of distributions	487,721	1,794,164
Amounts paid for units redeemed	(390,000)	(463,730)
Net increase from redeemable unit transactions	527,427	317,415
<b>Balance, end of year</b>	<b>\$ 15,765,907</b>	<b>\$ 15,238,480</b>

**Statement of Cash Flows**  
(all amounts in thousands)

	Year Ended December 31, 2017	Year Ended December 31, 2016
<b>Operating activities:</b>		
Increase (decrease) in net assets attributable to holders of redeemable units	\$ 274,706	\$ (1,013,019)
Adjustments for:		
Interest income	(83,894)	(86,293)
Dividend income	-	(1,367)
Net realized gain from investments	(286,519)	(1,682,211)
Net change in unrealized (appreciation) depreciation from investments	(409,871)	973,862
Non-cash distributions	487,721	1,794,164
Proceeds from sale of investments	6,522,542	4,326,597
Amounts paid for purchase of investments	(6,075,559)	(3,249,469)
External management fees payable	40	-
BCI cost recoveries payable	7,121	463
Other accounts payable	(497)	588
Interest received	84,285	85,172
Dividends received	114	1,395
	520,189	1,149,882
<b>Financing activities:</b>		
Proceeds from issue of redeemable units	60,000	-
Payments on redemption of redeemable units	(483,830)	(1,190,600)
	(423,830)	(1,190,600)
Net increase (decrease) in cash	96,359	(40,718)
Cash, beginning of year	81,429	122,147
<b>Cash, end of year</b>	<b>\$ 177,788</b>	<b>\$ 81,429</b>

*See accompanying notes to the financial statements.*

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND

<b>Schedule of Investments</b> (all amounts in thousands)				
	December 31, 2017		December 31, 2016	
	<u>Fair Value</u>	<u>Cost</u>	<u>Fair Value</u>	<u>Cost</u>
<b>Real Estate Investments<sup>1</sup>:</b>	\$ 15,334,800	\$ 8,935,265	\$ 15,175,443	\$ 9,187,939
<b>Equities:</b>				
Publicly traded	-	-	32,281	30,202
<b>Money Market Investments:</b>				
Units in BCI Pooled Investment Portfolio				
Fund ST1	24,716	24,741	36,506	36,506
Fund ST2	<u>141,888</u>	<u>141,986</u>	<u>7,767</u>	<u>7,773</u>
	166,604	166,727	44,273	44,279
<b>Total Investments</b>	<u>\$ 15,501,404</u>	<u>\$ 9,101,992</u>	<u>\$ 15,251,997</u>	<u>\$ 9,262,420</u>

<sup>1</sup> Real estate investments are held through private corporations, trusts, and limited partnerships funded by a combination of equity and debt [note 4 and note 8(a)]

*See accompanying notes to the financial statements.*

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

## 1. THE PORTFOLIO

British Columbia Investment Management Corporation ["BCI"] was established under the *Public Sector Pension Plans Act* as a trust company authorized to carry on trust business and investment management services. The address of BCI's registered office is at 750 Pandora Avenue, Victoria, British Columbia, Canada. These financial statements have been prepared by BCI and are the responsibility of BCI management.

Under the *Public Sector Pension Plans Act* and the *Pooled Investment Portfolios Regulation*, B.C. Reg. 447/99, BCI may establish and operate pooled investment portfolios "... in which money from trust funds, special funds or other funds, other public money and the money of government bodies and designated institutions may be combined in common for the purpose of investment by means of investment units of participation in a pooled investment portfolio." In addition, pooled investment portfolios previously established under the *Financial Administration Act* and the *Pooled Investment Portfolios Regulation* ("Regulations"), B.C. Reg. 84/86, were continued under the *Pooled Investment Portfolios Regulation*, B.C. Reg. 447/99, to be held in trust by BCI and invested by the Chief Investment Officer of BCI.

The Realpool Investment Fund [the "Fund"] was established on July 3, 1991 and invests in diversified Canadian income-producing properties including institutional-grade Canadian office, industrial, residential, retail, hospitality, and mixed-use properties, as well as publicly traded equities and money market instruments.

## 2. BASIS OF PRESENTATION

### (a) Statement of compliance

The financial statements have been prepared in compliance with International Financial Reporting Standards ("IFRS"). The financial statements were authorized for issue by the Chief Executive Officer/Chief Investment Officer on April 5, 2018.

### (b) Basis of consolidation

Real estate investments are held through subsidiaries of the Fund, which include private corporations, trusts, and limited partnerships funded by a combination of equity and debt. The Fund is an investment entity, and as such, does not consolidate the entities it controls. Instead, interests in subsidiaries are classified at fair value through profit and loss, and measured at fair value.

The Fund qualifies as an investment entity as it meets the following definition of an investment entity outlined in IFRS 10, *Consolidated Financial Statements* (IFRS 10):

- Obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services.
- Commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both.
- Measures and evaluates the performance of substantially all of its investments on a fair value basis.

No significant judgments or assumptions were made in determining that the Fund meets the definition of an investment entity as defined in IFRS 10.

### (c) Basis of measurement

The financial statements have been prepared on a historical cost basis, except for investments held at fair value through profit or loss ("FVTPL"), which are measured at fair value.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**2. BASIS OF PRESENTATION (continued)**

(d) Functional and presentation currency

These financial statements are presented in Canadian dollars, which is the Fund's functional currency.

(e) Use of estimates and judgment

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenue and expenses. In determining the fair value of some of its investments, management reviews and assesses external managers' estimates and assumptions regarding investment industry performance and prospects, as well as general business and economic conditions that prevail or are expected to prevail. By nature, these asset valuations are subjective and do not necessarily result in precise determinations. Financial results as determined by actual events could differ from those estimates and assumptions, and the difference could be material.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized in the period in which the estimates are revised and in any future period affected. Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next fiscal year is included in note 8 and relate to the determination of fair value of investments with significant unobservable inputs.

**3. SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

(a) Financial instruments

(i) Recognition and measurement

Financial instruments are required to be classified into one of the following categories: held-for-trading, FVTPL, available-for-sale, loans and receivables, assets held-to-maturity, and other financial liabilities. All financial instruments are measured at fair value on initial recognition. Measurement in subsequent periods depends on the classification of the financial instrument. Transaction costs are included in the initial carrying amount of financial instruments, except for financial instruments classified as held-for-trading or FVTPL in which case transaction costs are expensed as incurred.

Financial assets and financial liabilities held for trading or at fair value through profit or loss are recognized initially on the trade date, which is the date on which the Fund becomes a party to the contractual provisions of the instrument. Other financial assets and financial liabilities are recognized on the date on which they are originated. The Fund derecognizes a financial liability when its contractual obligations are discharged, cancelled or expire.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position only when the Fund has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

The Fund has not classified any financial instruments as available-for-sale or assets held to maturity.



BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**3. SIGNIFICANT ACCOUNTING POLICIES (continued)**

(a) Financial instruments (continued)

(ii) Fair value through profit and loss

Financial instruments classified as FVTPL are subsequently measured at fair value at each reporting period with changes in fair value recognized in the Statement of Comprehensive Income. The Fund's investments are designated as FVTPL.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of financial assets and liabilities traded in active markets (such as publicly traded marketable securities) is based on quoted market prices at the close of trading on the reporting date. The Fund uses the last traded market price for both financial assets and financial liabilities where the last traded price falls within that day's bid-ask spread. In circumstances where the last traded price is not within the bid-ask spread, management determines the point within the bid-ask spread that is most representative of fair value based on the specific facts and circumstances. The Fund's policy is to recognize transfers into and out of the fair value hierarchy levels as of the date of the event or change in circumstances giving rise to the transfer.

The fair value of financial assets and liabilities that are not traded in an active market is determined using valuation techniques. Valuation techniques also include the use of comparable recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and others commonly used by market participants and which make the maximum use of observable inputs.

(iii) Other financial liabilities

Other financial liabilities are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method. The Fund's other financial liabilities are comprised of other accounts payable, payable for redemption of units, and BCI cost recoveries payable.

(iv) Cash and cash equivalents

Cash comprises cash balances and bank deposits with maturities of three months or less.

(b) Redeemable units

The Fund classifies financial instruments issued as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. In accordance with the Regulations, the Fund is required to distribute, to holders of the Fund's redeemable units, the taxable income and taxable capital gains of the Fund at least annually. Accordingly, such units are classified as financial liabilities at FVTPL and measured at redemption amount Net Asset Value ("NAV"). Distributions to holders of redeemable units are recognized in comprehensive income when they are authorized and no longer at the discretion of BCI.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**3. SIGNIFICANT ACCOUNTING POLICIES (continued)**

(c) Issue and redemption of units

Participation in the Fund is expressed in units. The initial value of a unit of the Fund on inception was \$1 million. For each subsequent unit issuance and redemption, the unit value is determined by dividing the fair value of the net assets of the portfolio by the total number of units outstanding. Where the Fund invests in another BCI Fund, the unit issuances and redemptions are transacted on the same basis as client transactions. All unit transactions are recorded on a trade date basis.

(d) Income recognition

Interest income is recognized on an accrual basis using the effective interest method. Dividend income is recognized on the date that the right to receive payment is established, which for quoted equity securities is usually the ex-dividend date. Portfolio transactions are recorded on the trade date. Realized gains and losses arising from the sale of investments are determined on the average cost basis of the respective investments. The year-over-year change in the difference between the fair value and the cost of the investments held at year end is recognized as a net change in unrealized appreciation (depreciation). Commissions, stock exchange fees and other identifiable transaction costs that are directly attributable to the acquisition or disposal of an investment are expensed as incurred. Pursuit costs are charged to net income of the Fund in the period incurred.

(e) Income taxes

The Fund qualifies as an inter-vivos trust under the subsection 108(1) of the *Income Tax Act* (Canada). All of the Fund's net income for tax purposes and net capital gains realized in any period are required to be distributed to unitholders such that no income tax is payable by the Fund. As a result, the Fund does not record income taxes. Income taxes of the Fund's underlying investments that are taxable entities are accounted for in determining the fair value of the respective investments.

(f) Standards issued but not yet effective

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended December 31, 2017, and have not been applied in preparing these financial statements. None of these will have a significant effect on the financial statements of the Fund, with the possible exception of IFRS 9, *Financial Instruments*.

IFRS 9 deals with recognition, de-recognition, classification and measurement, impairment and hedge accounting of financial instruments and its requirements represent a significant change from the existing requirements in IAS 39, *Financial Instruments: Recognition and Measurement*, in respect of financial assets. The standard contains two primary measurement categories for financial assets: amortized cost and fair value. A financial asset would be measured at amortized cost if it is held within a business model whose objective is to hold assets in order to collect contractual cash flows, and the asset's contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding. All other financial assets would be measured at fair value. The standard eliminates the existing IAS 39 categories of held-to-maturity, available-for-sale and loans and receivables.

The effective date of this standard is January 1, 2018, but early adoption is permitted. Management is currently in the process of evaluating the potential effect of this standard. The standard is not expected to have a significant impact on the financial statements since the Fund's financial assets are currently measured at fair value or amortized cost.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**4. INVESTMENTS AT FAIR VALUE THROUGH PROFIT AND LOSS**

The Fund manages the following types of investments and determines fair value as follows:

- Real estate investments

Real estate investments consist of equity and debt investments in 136 wholly-owned (2016 – 156) and 8 partially owned (2016 – 11) subsidiary entities which are corporations, limited partnerships and trusts (all established in Canada). These subsidiaries qualify as investments and are not consolidated in the financial statements of the Fund but are instead reported at fair value.

The fair value of subsidiary entities (corporations, limited partnerships and trusts) is determined by the NAV of the entity, which is a sum of the fair value of the real estate properties and underlying entities, net of the fair value of issued mortgages and notes and the other short-term assets and liabilities. Fair value for the real estate properties and/or other entities held by the subsidiaries is primarily determined using discounted cash flows based on various factors such as operating income, discount rate and terminal capitalization rates.

The fair value of the debt investments in subsidiaries approximates their face value unless the face value of the debt exceeds the net assets available to repay the debt (i.e. the loan to the subsidiary is impaired). In these cases, the value of the loan is written down to the value of the available net assets.

- Equities

Equities consist of publicly traded shares. Fair value is based on quoted market prices.

- Money market investments

The Fund holds units in two BCI money market funds. The units of the money market funds are valued based on the sum of the fair value of the net assets of the funds.

**5. RELATED PARTY TRANSACTIONS**

The Fund's related parties include BCI, the Province of British Columbia and related entities, investments where the Fund has a controlling interest or significant influence, and other related entities for which the Fund provides investment management services. The Fund had the following transactions with related parties during the year:

- The Fund incurred cost recoveries from BCI, including indirect costs initially paid by BCI. These costs were recovered from the Fund through cost recoveries charged by BCI. BCI cost recoveries and the corresponding payable are disclosed in the Fund's Statement of Comprehensive Income and Statement of Financial Position.
- In 2015, a subsidiary of the Fund entered into a joint venture arrangement (50% co-owner) for the construction of a new office development in Victoria, B.C. BCI entered into an arm's length lease to rent office space as the primary tenant of the building. The lease commenced on March 1, 2018, for an initial term of twenty years with 3 five-year renewal options. As at December 31, 2017, minimum lease revenue to be received by the joint venture is estimated at \$204 million over twenty years excluding GST and other non-contractual amounts.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

## 6. REDEEMABLE UNITS

The Fund is authorized to issue an unlimited number of redeemable units. Redeemable units issued and outstanding represent the capital of the Fund. The Fund is not subject to any internally or externally imposed restrictions on its capital. BCI manages the capital of the Fund in accordance with the Fund's investment objectives, including managing the redeemable units to ensure a stable base to maximize returns to all investors, and managing liquidity in order to meet redemptions.

The following is a summary of the changes in redeemable units outstanding during the year:

	2017 (in number of units)	2016 (in number of units)
Outstanding, beginning of year	1,652.774	1,704.148
Issued	16.001	-
Issued on reinvestment of distributions	50.348	196.096
Consolidation of units	(50.348)	(196.096)
Redeemed	(41.683)	(51.374)
Outstanding, end of year	<u><u>1,627.092</u></u>	<u><u>1,652.774</u></u>

## 7. FINANCIAL RISK MANAGEMENT

### (a) Risk management framework

The investment objective of the Fund is to provide clients with exposure to a portfolio of Canadian real estate and real estate-related investments. The Fund's holdings are highly diversified by property type, geographic location, investment size, and investment risk. The Fund primarily concentrates on high-quality income-producing Canadian office, industrial, residential, retail, hospitality and mixed-use properties located in geographic regions that have strong and growing economies. The Fund's investment strategy is to be well diversified and to hold quality properties that will perform well across multiple economic cycles. Real estate investments are only made when there is a reasonable expectation that return objectives can be achieved over a ten-year horizon.

The Fund can invest in the following assets:

- eligible real estate investments for pension plans under the Pensions Benefits Standards Act (B.C.);
- real estate-related investments, including trust units, partnership interests, shares and debt;
- units in the external real estate managers' pooled funds provided such holdings are permissible investments for the Fund;
- derivative instruments for the purposes of synthetic indexing, risk control, lowering transaction costs, and/or liquidity management;
- BCI Canadian Money Market Funds ST1 and ST2; and/or government debt securities with a maximum term to maturity of one year, for cash management purposes.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**7. FINANCIAL RISK MANAGEMENT (continued)**

(a) Risk management framework (continued)

The following restrictions apply to the Fund's use of debt financing:

- it may only be used in a prudent manner for real estate and real estate-related investment;
- it may not be created if, as a result, the loan to value ratio of the Fund would exceed 35 percent.

As of December 31, 2017, the debt to market value ratio of the overall real estate portfolio was 21.65% [2016 - 20.54%].

BCI, as trustee of the Fund, has the power to vary the investments and assets of the Fund and reinvest proceeds realized from the investments of the Fund all within the bounds of the investment policies, rules and restrictions established for and governing the Fund.

The Fund's activities expose it to a variety of financial risks. For purposes of describing the financial risks of the Fund, the composition of the net assets held by the underlying corporations, trusts, limited partnerships, equities and money market funds and their investing activities have been considered. As at December 31, 2017, and December 31, 2016, the corporations, trusts and limited partnerships hold the following underlying net assets which make up the real estate assets of the Fund:

	December 31, 2017		December 31, 2016	
	Total	% of Total	Total	% of Total
Real estate properties	\$ 19,617,944	127.9	\$ 19,262,049	126.9
Direct private debt	152,277	1.0	134,507	0.9
Direct private equity	303,010	2.0	117,409	0.8
Mortgages	(1,412,458)	(9.2)	(1,481,751)	(9.8)
Notes payable	(3,065,900)	(20.0)	(2,611,014)	(17.2)
Other net assets	(260,073)	(1.7)	(245,757)	(1.6)
	<u>\$ 15,334,800</u>	<u>100.0</u>	<u>\$ 15,175,443</u>	<u>100.0</u>

(b) Credit risk

Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to meet their obligations to Fund's subsidiary entities. The Fund's credit risk is limited to the recorded amount of these obligations. To mitigate this risk, the Fund has a diverse set of tenants in a variety of industries, and the Fund performs ongoing credit evaluations of its customers and establishes allowances for potential losses.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**7. FINANCIAL RISK MANAGEMENT (continued)**

(c) Liquidity risk

Liquidity risk is the risk that the Fund will be unable to generate sufficient cash in a timely manner or at a reasonable price to meet commitments as they come due. The Fund is exposed to the liquidity risk associated with the requirement to redeem units. Redeemable units of the Fund may only be acquired by eligible clients or client groups in accordance with the Fund's purchasing limits that may be established by the Chief Investment Officer (CIO). In order to protect the interest of all clients, the CIO may also establish redemption limits for the Fund. The purchase and redemption limits may vary depending on market circumstances, client demand, and the liquidity of the underlying investments.

(d) Market risk

Market risk is the risk that changes in market prices, such as interest rates, foreign exchange rates and equity prices, will affect the Fund's income or the fair value of its holdings of financial instruments.

(i) Interest rate risk

Interest rate risk is the risk that the market value or cash flows of interest-bearing investments will fluctuate due to changes in market interest rates. The variable interest rate notes and fixed rate notes of the Fund are receivable from the underlying corporations, limited partnerships and trusts, so the Fund is not subject to interest rate risk on these financial instruments.

The mortgages of the underlying non-consolidated subsidiary corporations, trusts and limited partnerships bear interest rates up to 6.96% [2016 - 6.96%] with a weighted average rate of 2.58% [2016 - 2.66%]. They are due at various dates to 2026. Principal repayments on the mortgages are due as follows:

	<u>Principal Repayments</u>
2018	\$ 102,154
2019	26,711
2020	1,005,615
2021	264,233
2022	22,296
2023 and thereafter	5,619
	<u>\$ 1,426,628</u>

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**7. FINANCIAL RISK MANAGEMENT (continued)**

(d) Market risk (continued)

(i) Interest rate risk (continued)

The notes payable of the underlying non-consolidated corporations are unsecured and have the following terms and interest rates:

Issue	Maturity date	Fixed Interest rate	2017	2016
			Fair Value	Fair Value
Series 6	January 5, 2018	5.65%	\$ 200,001	\$ 209,004
Series 8	March 7, 2019	2.96%	506,119	516,120
Series 9	June 19, 2017	2.65%	-	251,989
Series 10	June 29, 2022	3.51%	260,531	266,417
Series 11	August 2, 2018	2.79%	503,440	511,419
Series 12	June 3, 2021	2.10%	346,931	352,163
Series 13	June 3, 2025	2.84%	500,479	503,902
Series A	August 11, 2022	2.15%	245,857	-
Series B	March 31, 2027	3.00%	502,542	-
			<u>\$ 3,065,900</u>	<u>\$ 2,611,014</u>

As at December 31, 2017, if the interest rates increased/decreased by 1% with other variables held constant, the fair value of the mortgages and notes payable would decrease/increase by \$112,858, respectively.

(ii) Real estate risk

The Fund has identified the following risks associated with the real estate portfolio:

- The cost of development projects may increase if there are delays in the planning process. The Fund uses advisers who are experts in the specific planning requirements in the project's location in order to reduce the risks that may arise in the planning process.
- The exposure of the fair values of the Fund to market and occupier fundamentals.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**7. FINANCIAL RISK MANAGEMENT (continued)**

(d) Market risk (continued)

(iii) Other valuation risk

As at December 31, underlying real estate investment properties held by the Fund are diversified across the following property sectors:

	2017		2016	
	Total	% of Total	Total	% of Total
<b>Real estate properties</b>				
Retail	\$ 2,891,100	14.8	\$ 1,936,100	10.1
Office	8,268,525	42.1	8,407,825	43.6
Industrial	1,965,860	10.0	1,857,995	9.6
Residential	3,289,090	16.8	3,264,260	16.9
Retirement homes	264,700	1.3	44,300	0.2
Hospitality	-	-	1,031,544	5.5
Land lease communities	1,387,287	7.1	1,431,995	7.4
Land held for development / property under development	1,551,382	7.9	1,288,030	6.7
<b>Total real estate properties</b>	<b>\$ 19,617,944</b>	<b>100.0</b>	<b>\$ 19,262,049</b>	<b>100.0</b>

As at December 31, real estate investment properties held by the Fund are diversified across the following geographic regions in Canada:

	2017		2016	
	Total	% of Total	Total	% of Total
<b>Real estate properties</b>				
British Columbia	\$ 5,398,618	27.5	\$ 4,307,902	22.4
Alberta	5,219,479	26.6	5,798,011	30.1
Saskatchewan	36,220	0.2	149,019	0.8
Manitoba	276,410	1.4	278,330	1.4
Ontario	7,813,569	39.8	7,705,261	40.0
Quebec	602,398	3.1	668,509	3.5
Prince Edward Island	-	-	6,892	-
New Brunswick	11,600	0.1	39,208	0.2
Nova Scotia	259,650	1.3	291,753	1.5
Newfoundland	-	-	17,164	0.1
<b>Total real estate properties</b>	<b>\$ 19,617,944</b>	<b>100.0</b>	<b>\$ 19,262,049</b>	<b>100.0</b>



BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**8. FAIR VALUE MEASUREMENT**

(a) Fair value hierarchy

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Fund determines fair values using other valuation techniques.

For financial instruments that trade infrequently and have little price transparency, fair value is less objective and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

The Funds measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

Level 1: Quoted market prices (unadjusted) in active markets for identical instruments.

Level 2: Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.

Level 3: Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly unobservable.

The table below shows investments measured at fair value at the reporting date by the level in the fair value hierarchy into which the fair value measurement is categorized. All fair value measurements are recurring.

Type of investment	2017				
	Quoted prices in active markets [Level 1]	Significant observable inputs [Level 2]	Significant unobservable inputs [Level 3]	Total	
Money market investments	\$ -	\$ 166,604	\$ -	\$	166,604
Real estate investments	-	-	15,334,800		15,334,800
Total Investments	\$ -	\$ 166,604	\$ 15,334,800	\$	15,501,404

  

Type of investment	2016				
	Quoted prices in active markets [Level 1]	Significant observable inputs [Level 2]	Significant unobservable inputs [Level 3]	Total	
Money market investments	\$ -	\$ 44,273	\$ -	\$	44,273
Public equities	32,281	-	-		32,281
Real estate investments	-	-	15,175,443		15,175,443
Total Investments	\$ 32,281	\$ 44,273	\$ 15,175,443	\$	15,251,997

During 2017 and 2016, there were no transfers between Levels 1, 2 or 3.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**8. FAIR VALUE MEASUREMENT (continued)**

(a) Fair value hierarchy (continued)

The carrying amount of the investments in money market funds also approximates fair value as they are measured at the redemption amount and are classified as Level 2 in the fair value hierarchy.

The following tables show a reconciliation from the beginning balances to the ending balances for fair value measurements in Level 3 of the fair value hierarchy.

2017	
	Real estate investments
Opening balance, January 1, 2017	\$ 15,175,443
Total gains recognized in profit or loss	284,131
Purchases	3,563,965
Sales	(4,100,771)
Total unrealized gains (losses) for the period included in the profit or loss	412,032
Closing balance, December 31, 2017	<u>\$ 15,334,800</u>

2016	
	Real estate investments
Opening balance, January 1, 2016	\$ 14,811,877
Total gains recognized in profit or loss	1,684,306
Purchases	2,326,983
Sales	(2,668,409)
Total unrealized gains (losses) for the period included in the profit or loss	(979,314)
Closing balance, December 31, 2016	<u>\$ 15,175,443</u>

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**8. FAIR VALUE MEASUREMENT (continued)**

**(b) Valuation models**

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The Fund uses widely recognized valuation methods for determining the fair value of common and more simple financial instruments such as money market instruments that use only observable market data which requires little management judgment and estimation. Valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which observable market prices exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other factors used in estimating discount rates, and money market prices.

Observable prices and model inputs are usually available in the market for equities. The availability of observable market prices and model inputs reduces the need for management judgment and estimation and reduces the uncertainty associated with the determination of fair values. The availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

For more complex instruments, such as private equity and debt, the Fund uses proprietary valuation models, which are usually developed from recognized valuation models. Some or all of the significant inputs into these models may not be observable in the market, and are derived from market prices or rates or are estimated based on assumptions. Valuation models that employ significant unobservable inputs require a higher degree of management judgment and estimation in the determination of fair value. Management judgment and estimation are usually required for the selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instrument being valued, determination of the probability of counterparty default and prepayments and selection of appropriate discount rates.

Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties, to the extent that the Fund believes that a third party market participant would take them into account in pricing a transaction. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Fund and the counterparties where appropriate.

**(c) Valuation framework**

The Fund has an established framework with respect to the measurement of fair values and applies the following specific controls in relation to the determination of fair values:

- verification of observable pricing inputs;
- appraisal of domestic real estate properties once every ten to eighteen months by accredited independent appraisers;
- analysis and investigation of significant valuation movements for real estate investments; and
- review of unobservable inputs and valuation adjustments for real estate investments.

When third party information, such as broker quotes or pricing services, is used to measure fair value, then BCI management assesses and documents the evidence obtained from the third parties to support the conclusion that such valuations are appropriate. This includes:

- verifying that the broker or pricing service is approved by the Fund for use in pricing the relevant type of financial instrument;
- understanding how the fair value has been arrived at and the extent to which it represents actual market transactions;
- when prices for similar instruments are used to measure fair value, how these prices have been adjusted to reflect the characteristics of the instrument subject to measurement; and
- if a number of quotes for the same financial instrument have been obtained, then how fair value has been determined using those quotes.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**8. FAIR VALUE MEASUREMENT (continued)**

(d) Significant unobservable inputs used in measuring fair value

2017				
	Fair Value	Valuation Technique	Unobservable Input	Sensitivity to Change in Significant Unobservable Input
Real estate investments	\$15,334,800	Unadjusted Net Asset Value	Net Asset Value is compiled by the investment managers based on various unobservable inputs as applicable to each underlying investment.	The estimated fair value would increase (decrease) if the following changes were made to valuations of the underlying investments in the investees and unlisted private equity investee funds: - the discount rates were lower (higher); - the EV/EBITDA multiples were higher (lower); or - a change in the annual revenue growth rate is accompanied by a directionally similar change in the EBITDA margin.
2016				
	Fair Value	Valuation Technique	Unobservable Input	Sensitivity to Change in Significant Unobservable Input
Real estate investments	\$15,175,443	Unadjusted Net Asset Value	Net Asset Value is compiled by the investment managers based on various unobservable inputs as applicable to each underlying investment.	The estimated fair value would increase (decrease) if the following changes were made to valuations of the underlying investments in the investees and unlisted private equity investee funds: - the discount rates were lower (higher); - the EV/EBITDA multiples were higher (lower); or - a change in the annual revenue growth rate is accompanied by a directionally similar change in the EBITDA margin.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**8. FAIR VALUE MEASUREMENT (continued)**

Significant unobservable inputs are developed as follows:

(i) Enterprise Value ("EV") and earnings before interest, tax, depreciation and amortization ("EBITDA") multiples:

Represent amounts that market participants would use when pricing the investments. EV and EBITDA multiples are selected from comparable public companies based on geographic location, industry, size, target markets, and other factors that management considers to be reasonable. The traded multiples for the comparable companies are determined by dividing the EV of the company by its EBITDA and further discounted for considerations such as the lack of marketability and other differences between the comparable peer group and specific company.

(ii) Discount rate:

Represents the discount rate applied to the expected future cash flows of each underlying real estate investment property or investments. BCI management assesses both the risk premium and the appropriate risk-free rate based on the economic environment in which the investee operates to determine the discount rate. The discount rate is adjusted for such matters as liquidity differences, credit and market factors. Cash flows used in the discounted cash flow model are based on projected cash flows or earnings of the respective underlying real estate property or investment.

(e) Effects of unobservable input on fair value measurement

Although the Fund believes its estimates of fair value in Level 3 are appropriate, the use of different methodologies or assumptions could lead to different measurements of fair value and net assets attributable to holders of redeemable units. The following table shows how the net assets attributable to holders of redeemable units would change if the valuation of the real estate investments were calculated by adjusting the respective net assets and debt by 10%.

	2017	2016
Favourable	\$ 1,533,480	\$ 1,517,543
Unfavourable	\$ (1,533,480)	\$ (1,517,543)

(f) Other financial instruments

The carrying value of receivable from issuance of redeemable units, dividends receivable, other accounts payable, payable for the redemption of redeemable units and BCI cost recoveries payable approximates their fair value given their short-term nature.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**9. INVOLVEMENT WITH SUBSIDIARIES AND ASSOCIATES**

The Fund's investments are held primarily through 136 wholly owned and 8 partially owned subsidiary entities, all of which constitute structured entities. Structured entities are entities that have been designed so that voting or other similar rights are not the dominant factor in determining who controls the entity. These structured entities have been set up by BCI to manage credit and other risks that may arise in the course of administering the underlying investments.

During 2017 and 2016, the Fund provided financial support to subsidiaries or associates for investment and operation activities and has committed to providing financial support under loan arrangements or shareholders' resolutions as needed.

**10. INVOLVEMENT WITH STRUCTURED ENTITIES**

In addition to the entities in note 9, the Fund holds interests in other structured entities which are comprised of a directly held trust and two directly held investee money market funds. All of these entities are organized as unit trusts. The entities have been constituted to manage assets on behalf of third party investors and are financed through the issuance of units to investors. The table below sets out the interests held by the Fund in these other structured entities:

Entity	2017			2016		
	Number of Entities as at December 31, 2017	Total Net Assets of Entities December 31, 2017	Carrying Amount December 31, 2017	Number of Entities as at December 31, 2016	Total Net Assets of Entities December 31, 2016	Carrying Amount December 31, 2016
Investment in trusts	3	\$ 425,330	\$ 425,330	3	\$ 551,086	\$ 551,086
Unlisted managed funds	2	6,195,002	166,604	2	3,586,017	44,273
		\$ 6,620,332	\$ 591,934		\$ 4,137,103	\$ 595,359

The carrying amount of the investments held in these underlying funds represents the Fund's maximum exposure to loss. The Fund has commitments to provide financial support to wholly owned subsidiaries to fund day-to-day operations and investment activity. During 2017, the Fund provided \$127,695 (2016 - \$26,830) in financial support to the structured entities for investment activities.

**11. TAXES**

The net capital losses for the Fund were nil as at December 31, 2017 (2016 - \$2,249).

By order of the British Columbia Supreme Court, and affirmed on appeal by the British Columbia Court of Appeal, the investment pools managed by BCI have been declared to be immune from the application of the Excise Tax Act. Those same pools have been declared to be bound to certain reciprocal tax treaties between Canada and British Columbia which may require them to pay amounts in lieu of GST and which may entitle them to obtain full refunds of any amounts paid.

BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION  
REALPOOL INVESTMENT FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2017  
(all amounts in thousands except units)

**12. COMMITMENTS AND CONTINGENCIES**

The Fund, its wholly owned corporations and limited partnerships have property purchase and development commitments of \$354,791 [2016 - \$335,210], unfunded commitments to certain investment funds of nil [2016 - nil], commercial purchasing card lines of credit of \$950 [2016 - \$2,800], and have issued letters of credit totalling \$86,492 [2016 - \$98,796]. Certain investments of the Fund may, in the normal course of business activities, be involved in disputes with third parties. BCI management assesses the likelihood of loss relating to any disputes and has determined that such disputes would not have a material impact on the NAV of the Fund.

**13. SUBSEQUENT EVENTS**

On January 5, 2018, a subsidiary of the Fund repaid \$200 million on the maturity of Series 6 notes payable.



**BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION**

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