Mortgages: Mezzanine Mortgage & US Mortgage Opportunity - Pooled Fund Financial Statements

DECEMBER 2018

British Columbia Investment Management Corporation

Mezzanine Mortgage Fund
US Mortgage Opportunity Fund

British Columbia Investment Management Corporation
Pooled Investment Portfolios

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

British Columbia Investment Management Corporation (BCI) manages Pooled Investment Portfolios on behalf of governing fiduciaries such as pension fund trustees and other public sector clients. This report contains the financial statements for the following Pooled Investment Portfolios for the year ended December 31, 2018:

Mezzanine Mortgage Fund
US Mortgage Opportunity Fund

The financial statements of the Pooled Investment Portfolios have been prepared by management of BCI and approved by the Chief Investment Officer/Chief Executive Officer. All of 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 judgement 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 Pooled Investment Portfolios, 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 Pooled Investment Portfolios.   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.

BCI's external auditors, KPMG LLP, have full and unrestricted access to the Audit Committee and BCI management. KPMG LLP discusses with management and the Committee the results of their audit of the Pooled Investment Portfolios' financial statements and related findings with respect to such audits. Each of the Pooled Investment Portfolio financial statements is audited by KPMG LLP in accordance with Canadian generally accepted auditing standards. KPMG LLP has performed such tests and other procedures as they considered necessary to express an opinion on the Pooled Investment Portfolio financial statements.

[S] Gordon J. Fyfe	[S] Lawrence E. Davis
Gordon J. Fyfe	Lawrence E. Davis
Chief Executive Officer / Chief Investment Officer	Senior Vice President, Finance

Victoria, British Columbia
July 4, 2019

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INDEPENDENT AUDITORS' REPORT

To the Unitholders of the following funds managed by British Columbia Investment Management Corporation:

Mezzanine Mortgage Fund

US Mortgage Opportunity Fund (collectively, the "Funds")

Opinion

We have audited the financial statements of the Funds, which comprise:

- the statements of financial position as at December 31, 2018
- the statements of comprehensive income/(loss) for the year then ended
- the statements of changes in net assets attributable to holders of redeemable units for the year then ended
- the statements of cash flows for the year then ended
- and notes to the financial statements, including a summary of significant accounting policies.

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Funds as at December 31, 2018, and their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audits in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "***Auditors' Responsibilities for the Audit of the Financial Statements***" section of our auditors' report.

We are independent of the Funds in accordance with the ethical requirements that are relevant to our audits of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Responsibilities of The Manager and Those Charged with Governance for the Financial Statements

The Manager is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as the Manager determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Manager is responsible for assessing the Funds' abilities to continue as going concerns, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the Manager either intends to liquidate the Funds or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Funds' financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Funds' internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Manager.

- Conclude on the appropriateness of the Manager's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Funds' ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Funds to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audits and significant audit findings, including any significant deficiencies in internal control that we identify during our audits.

KPMG LLP

Chartered Professional Accountants

Vancouver, Canada
July 4, 2019

MEZZANINE MORTGAGE FUND

Statement of Financial Position
(all amounts in thousands *except number of units*)

	Note	December 31, 2018	December 31, 2017
Assets			
Investments		$ 124,103	$ 192,646
		124,103	192,646
Liabilities			
BCI cost recoveries payable	4	365	189
Other accounts payable		12	11
		377	200
Net assets attributable to holders of redeemable units		**$ 123,726**	**$ 192,446**
Number of redeemable units outstanding	5	*22.583*	*39.543*
Net assets attributable to holders of redeemable units per unit		**$ 5,479**	**$ 4,867**

Statement of Comprehensive Income/(Loss)
(all amounts in thousands)

	Note	Year Ended December 31, 2018	Year Ended December 31, 2017
Revenue:			
Interest income		$ 3	$ 2
Change in fair value of investments:			
Net realized gain		31,641	4,874
Net change in unrealized appreciation		(13,116)	11,426
Total revenue		18,528	16,302
Expenses:			
Administrative fees		28	22
BCI cost recoveries	4	1,020	619
Total operating expenses		1,048	641
Increase in net assets attributable to holders of redeemable units from operations excluding distributions		17,480	15,661
Distributions to holders of redeemable units:			
From net realized gains on investments		(30,399)	(4,422)
		(30,399)	(4,422)
Increase (decrease) in net assets attributable to holders of redeemable units		$ (12,919)	$ 11,239

[S] Gordon J. Fyfe

Gordon J. Fyfe
Chief Executive Officer
Chief Investment Officer

See accompanying Notes to the Financial Statements.

MEZZANINE MORTGAGE FUND

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

	Year Ended December 31, 2018	Year Ended December 31, 2017
Balance, beginning of year	$ 192,446	$ 179,035
Increase (decrease) in net assets attributable to holders of redeemable units	(12,919)	11,239
Redeemable unit transactions:		
Proceeds from units issued	8,300	15,250
Reinvestment of distributions	30,399	4,422
Amounts paid for units redeemed	(94,500)	(17,500)
Net increase (decrease) from redeemable unit transactions	(55,801)	2,172
Balance, end of year	**$ 123,726**	**$ 192,446**

Statement of Cash Flows
(all amounts in thousands)

	Year Ended December 31, 2018	Year Ended December 31, 2017
Operating activities:		
Increase (decrease) in net assets attributable to holders of redeemable units	$ (12,919)	$ 11,239
Adjustments for:		
Interest income	(3)	(2)
Net realized gain from investments	(31,641)	(4,874)
Net change in unrealized appreciation of investments	13,116	(11,426)
Non cash distributions	30,399	4,422
Proceeds from sale of investments	96,163	18,177
Amounts paid for purchase of investments	(9,095)	(15,418)
BCI cost recoveries	176	131
Other accounts payable	1	(1)
Interest received	3	2
	86,200	2,250
Financing activities:		
Proceeds from issue of redeemable units	8,300	15,250
Payments on redemption of redeemable units	(94,500)	(17,500)
	(86,200)	(2,250)
Cash, beginning and end of year	$ -	$ -

See accompanying Notes to the Financial Statements.

MEZZANINE MORTGAGE FUND

Schedule of Investments
as at December 31
(all amounts in thousands)

	2018		2017	
	Fair Value	**Cost**	**Fair Value**	**Cost**
Mortgage Investments[1]:	$ 123,945	$ 79,068	$ 192,593	$ 134,600
Money Market Investments:				
Units in BCI Pooled Investment Portfolio:				
Fund ST1	158	158	53	53
Total Investments	$ 124,103	$ 79,226	$ 192,646	$ 134,653

[1] The mortgage investments are held through private corporations.

See accompanying Notes to the Financial Statements.

MEZZANINE MORTGAGE FUND

Financial Risk Management Discussion
as at December 31

The investment objectives, eligible investments and general information on the financial risks related to the Mezzanine Mortgage Fund are described in note 6 of the financial statements. The information contained in this Financial Risk Management Discussion pertains specifically to the Mezzanine Mortgage Fund.

The Fund holds its mortgage investments through private corporations. The private corporations hold the following net assets:

(in 000s)	2018 Total	2018 % of Total	2017 Total	2017 % of Total
Fixed-Rate Mortgages	$ 62,349	50.3 %	$ 123,002	63.9 %
Variable-Rate Mortgages	8,000	6.5 %	-	- %
Other Mortgage Investments	52,091	42.0 %	66,662	34.6 %
BCI Money Market Funds	1,118	0.9 %	2,141	1.1 %
Other Net Receivables	387	0.3 %	789	0.4 %
	$ 123,945	100.0 %	$ 192,593	100.0 %

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 and their investing activities have been considered. The other mortgage investments consist of limited partnerships and co-investment/parallel investment agreements and often involve equity participation.

Financial Risk Management Discussion (continued)
as at December 31

Credit Risk

The Fund invests in leveraged properties where the possibility of a borrower defaulting on payment obligations is higher than conventional mortgages. In the event of a default, the Fund may hold assets that otherwise would not be permitted provided the holdings are approved by the Chief Investment Officer and accepting the assets is deemed to be in the best interest of the Fund participants.

Some of the mortgages and other mortgage investments may have a higher loan-to-value ratio than traditional first mortgages. In exchange for the higher levels of risk associated with mortgages of this nature, the Mezzanine Mortgage Fund requires additional compensation and/or additional security provisions. As such, mortgage terms may involve equity participation in the development project to achieve higher rates of return and compensate for additional credit risk.

The fair value of mortgage investments as disclosed in the Schedule of Investments represents the Fund's maximum exposure to credit risk.

Liquidity Risk

The Fund's financial assets include unlisted mortgage investments, which are generally illiquid. As a result, the Fund may not be able to liquidate some of its investments in these instruments in due time to meet its obligations when they become due. However, the CIO may obtain funding from unitholders of the Fund through additional unit issuances to meet the Fund's ongoing liquidity requirements.

The Fund's liabilities are due within three months of the year-end of the Fund.

MEZZANINE MORTGAGE FUND

**Financial Risk Management Discussion (continued)
as at December 31**

Interest Rate Risk

The Fund invests in mortgages with terms ranging from 1 to 5 years. Mezzanine mortgages may have fixed or floating interest rates. The duration of these fixed and floating rate mortgages is 1.2 years (2017 - 1.4 years). Mortgage terms may involve equity participation in the development project to achieve higher internal rates of return.

As at December 31, the Fund invested in mortgages with the following terms to maturity:

MORTGAGES BY MATURITY DATE (in 000s)	2018 Total	2018 Average Effective Yield	2017 Total	2017 Average Effective Yield
Floating Rate Mortgages:				
1 to 5 years	$ 8,000	n/a %	$ -	n/a %
Fixed Rate Mortgages:				
Within 1 year	13,387	10.88 %	41,839	9 %
1 to 5 years	48,962	12.36 %	$ 81,163	11.72 %
Total Fixed and Floating Mortgages	$ 70,349	12.05 %	$ 123,002	10.80 %

All of the mortgages have a fixed term open to repayment. All of the mortgages except for one are subordinate to other BCI mortgages which require repayment in full before the mortgage in this fund can be repaid. Interest on variable rate mortgages is based on bank prime lending rates plus a risk and liquidity premium. Therefore, they do not have significant exposure to interest rate risk. As at December 31, 2018 if the interest rate had increased/decreased by 1 percent, holding all other variables constant, net assets would have decreased/increased by $863,000 (2017 - $1,754,000) representing 0.70% (2017 - 0.9%) of the Fund's net assets.

**Financial Risk Management Discussion (continued)
as at December 31**

Currency Risk

The Fund is not exposed to significant currency risk since the Fund's net financial assets and liabilities are denominated in Canadian dollars.

Other Price Risk

Mortgages by Industry Sector

Investments in the Fund are diversified across industry sectors. Sectors to which the Fund had exposure as at December 31 are as follows:

INDUSTRY SECTOR (in 000s)	2018 Total	2018 % of Total	2017 Total	2017 % of Total
Residential	$ 70,349	57.5 %	$ 123,002	64.9 %
Total Fixed-Rate and Variable-Rate Mortgages	70,349	57.5 %	123,002	64.9 %
Total Other Mortgage Investments in Residential Properties	52,091	42.5 %	66,662	35.1 %
	$ 122,440	100.0 %	$ 189,664	100.0 %

INDUSTRY SECTOR (Number of Mortgages)	2018 Total	2018 % of Total	2017 Total	2017 % of Total
Residential	6	46.2 %	7	43.7 %
Total Fixed-Rate and Variable-Rate Mortgages	6	46.2 %	7	43.7 %
Total Other Mortgage Investments in Residential Properties	7	53.8 %	9	56.3 %
	13	100.0 %	16	100.0 %

MEZZANINE MORTGAGE FUND

Financial Risk Management Discussion (continued)
as at December 31

Other Price Risk (continued)

As at December 31, 2018 and 2017, had the fair value of the investments increased or decreased by 10%, with all other variables held constant, net assets attributable to holders of redeemable units would have increased or decreased by approximately $12,410,000 (2017 - $19,265,000) or 10.0% (2017 – 10.0%) of net assets attributable to holders of redeemable units.

Actual trading results may differ from the above sensitivity analysis and the difference could be material.

Fair Value Measurement Discussion
as at December 31

Fair Value Hierarchy

As described in note 7 of the financial statements, a three-tier hierarchy is used as a framework for disclosing fair value based on inputs used to value the Fund's financial instruments.

The tables below analyze financial instruments measured at fair value at the reporting date by the level in the fair value hierarchy into which the fair value measurement is categorized. The amounts are based on the values recognized in the Statement of Financial Position. All fair value measurements below are recurring.

	2018			
(in 000s)	Level 1 (Quoted Price in Active Market)	Level 2 (Significant Observable Inputs)	Level 3 (Significant Unobservable Inputs)	Total
Net Investment-Related Receivables	$ -	$ 387	$ -	$ 387
BCI Money Market Funds	1,276	-	-	1,276
Fixed-Rate Mortgages	-	62,349	-	62,349
Variable-Rate Mortgages	-	8,000	-	8,000
Other Mortgage Investments	-	-	52,091	52,091
Total Investments	$ 1,276	$ 70,736	$ 52,091	$ 124,103

	2017			
(in 000s)	Level 1 (Quoted Price in Active Market)	Level 2 (Significant Observable Inputs)	Level 3 (Significant Unobservable Inputs)	Total
Net Investment-Related Receivables	$ -	$ 788	$ -	$ 788
BCI Money Market Funds	2,194	-	-	2,194
Fixed-Rate Mortgages	-	123,002	-	123,002
Other Mortgage Investments	-	-	66,662	66,662
Total Investments	$ 2,194	$ 123,790	$ 66,662	$ 192,646

MEZZANINE MORTGAGE FUND

Fair Value Measurement Discussion (continued)
as at December 31

Fair Value Hierarchy (continued)

During 2018 and 2017, there were no significant transfers between Level 1 and Level 2.

The carrying amount of the Fund's net assets attributable to holders of redeemable units also approximates fair value as they are measured at redemption amount and are classified as Level 2 in the fair value hierarchy.

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

	2018	2017
(in 000s)	Other Mortgage Investments	Other Mortgage Investments
Balance, beginning of year	$ 66,662	$ 52,949
Total losses recognized in profit or loss	(3,127)	(2,512)
Purchases	171	17,818
Sales	(11,615)	(1,593)
Balance, end of year	$ 52,091	66,662
Total unrealized losses for the year included in profit or loss relating to financial assets and liabilities held at the reporting date	$ (2,557)	(4,620)

During 2018 and 2017, there were no significant transfers into or out of Level 3.

Fair Value Measurement Discussion (continued)
as at December 31

Significant Unobservable Inputs Used in Measuring Fair Value

The table below sets out information about significant unobservable inputs used at year-end in measuring the fair value of other mortgage investments categorized as Level 3 in the fair value hierarchy as at December 31:

	2018					
	Fair Value (in 000s)	Valuation Technique	Unobservable Input	Amount / Range	Weighted Average	Sensitivity to Change in Significant Unobservable Input
Other Mortgage Investments	$ 38,527	Net Asset Value	Net Asset Value	$ 38,527	N/A	The estimated fair value would increase (decrease) if the net asset value was higher (lower).
	$ 13,564	Discounted Cash Flow	Discount rate	12%-20%	13%	The estimated fair value would increase (decrease) if the discount rate was lower (higher).

MEZZANINE MORTGAGE FUND

Fair Value Measurement Discussion (continued)
as at December 31

Significant Unobservable Inputs Used in Measuring Fair Value (continued)

	2017				
	Fair Value (in 000s)	Valuation Technique	Unobservable Input	Amount / Range	Sensitivity to Change in Significant Unobservable Input
Other Mortgage Investments	$ 42,109	Net Asset Value	Net Asset Value	$ 42,109	The estimated fair value would increase (decrease) if the net asset value was higher (lower).
	$ 24,553	Discounted Cash Flow	Discount rate	9%-10%	The estimated fair value would increase (decrease) if the discount rate was lower (higher).

Significant unobservable inputs are developed as follows:

(i) Net Asset Value:
Represents the net asset value of the unlisted mortgage investments investee funds. BCI management values these funds primarily based on the latest available financial information provided by their general partners.

(ii) Discount rate:
Represents the discount rate applied to the expected future cash flows. For the discount rates used, BCI management assesses both the risk premium and the appropriate risk-free rate based on the economic environment in which the investee entity operates. The discount rate is adjusted for such matters as liquidity differences, credit and market factors. The estimated future cash flows are then discounted using the discount rate determined. Cash flows used in the discounted cash flow model are based on projected cash flows or earnings of the respective investee entity.

Fair Value Measurement Discussion (continued)
as at December 31

Effects of Unobservable Inputs on Fair Value Measurement

Although BCI believes that 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 net assets attributable to holders of redeemable units would change if the valuations of other mortgage investments were calculated by adjusting the respective other mortgage investments' net assets by 10%.

(in 000s)	2018	2017
Favourable	$ 5,200	$ 6,700
Unfavourable	$ (5,200)	$ (6,700)

MEZZANINE MORTGAGE FUND

Involvement with Structured Entities as at December 31

The Fund's investments are held primarily through 4 intermediary holding corporations, 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 legal, tax and other risks that may arise in the course of administering the underlying investments. The carrying amount of these entities, approximately $123,945,000 (2017 - $192,593,000), is shown under Investments in the Statement of Financial Position.

In addition, the Fund holds interests in other structured entities, both directly and indirectly (i.e. through the intermediary holding corporations). The other structured entities are comprised of directly held investee money market funds organized as unit trusts and indirectly held investee funds organized as limited partnerships, co-investments, syndicate investments and equity participation investments. All of these investee funds have been constituted to manage assets on behalf of third party investors and are financed through the issuance of units to investors or capital contributions made by the investors. Accordingly, the Fund's interest in these entities is reflected through the holding of trust units, partnership units or a partnership interest. The tables below set out the direct and indirect interests held by the Fund in these other structured entities:

	December 31, 2018		
Entity	Number of Investee Funds	Total Net Assets of Investee Funds (in 000s)	Carrying Amount Included in Investments in the Statement of Financial Position (in 000s)
Investee money market funds administered by BCI	1	$ 1,699,706	$ 1,276
Unlisted mortgage investments investee funds administered by third party managers	7	$ 252,837	$ 52,091

Involvement with Structured Entities (continued) as at December 31

	December 31, 2017		
Entity	Number of Investee Funds	Total Net Assets of Investee Funds (in 000s)	Carrying Amount Included in Investments in the Statement of Financial Position (in 000s)
Investee money market funds administered by BCI	1	$ 923,072	$ 2,194
Unlisted mortgage investments investee funds administered by third party managers	9	$ 378,174	$ 66,662

The carrying amount of the investments held in these underlying funds represents the Fund's maximum exposure to loss. During 2018 and 2017, the Fund did not provide financial support to these structured entities and has no intention of providing financial or other support.

US MORTGAGE OPPORTUNITY FUND

Statement of Financial Position
(all amounts in thousands *except number of units*)

	Note	December 31, 2018	December 31, 2017
Assets			
Other accounts receivable		$ 21,353	$ -
Investments		576,622	60,755
		597,975	60,755
Liabilities			
BCI cost recoveries payable	4	868	50
Other accounts payable		11	11
		879	61
Net assets attributable to holders of redeemable units		**$ 597,095**	**$ 60,694**
Number of redeemable units outstanding	5	*24,862.053*	*2,816.449*
Net assets attributable to holders of redeemable units per unit		**$ 24**	**$ 22**
Unfunded committed capital	*6*		

Statement of Comprehensive Income/(Loss)
(all amounts in thousands)

	Note	Year Ended December 31, 2018	Year Ended December 31, 2017
Revenue:			
Interest income		$ 29,489	$ -
Foreign exchange loss		(44)	-
Change in fair value of investments			
Net realized gain		376	-
Net change in unrealized appreciation of investments		28,873	394
Total revenue		58,694	394
Expenses:			
BCI cost recoveries	4	4,899	51
Administrative fees		231	107
Pursuit cost		685	621
Total operating expenses		5,815	779
Increase (decrease) in net assets attributable to holders of redeemable units		$ 52,879	$ (385)

[S] Gordon J. Fyfe

Gordon J. Fyfe
Chief Executive Officer
Chief Investment Officer

See accompanying Notes to the Financial Statements.

US MORTGAGE OPPORTUNITY FUND

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

	Year Ended December 31, 2018	Year Ended December 31, 2017
Balance, beginning of year	$ 60,694	$ 8
Increase (decrease) in net assets attributable to holders of redeemable units	52,879	(385)
Redeemable unit transactions:		
Proceeds from units issued	502,179	61,071
Amounts paid for units redeemed	(18,657)	-
Net increase from redeemable unit transactions	483,522	61,071
Balance, end of year	**$ 597,095**	**$ 60,694**

Statement of Cash Flows
(all amounts in thousands)

	Year Ended December 31, 2018	Year Ended December 31, 2017
Operating activities:		
Increase (decrease) in net assets attributable to holders of redeemable units	$ 52,879	$ (385)
Adjustments for:		
Effect of exchange rate changes on cash	44	-
Interest income	(29,489)	-
Net realized gain from investments	(376)	-
Net change in unrealized appreciation of investments	(28,873)	(394)
Proceeds from sale of investments	29,814	629
Amounts paid for purchase of investments	(516,431)	(60,980)
Other accounts receivable	(21,353)	-
BCI cost recoveries payable	818	50
Other accounts payable	-	9
Interest received	29,489	-
	(483,478)	(61,071)
Financing activities:		
Proceeds from issue of redeemable units	502,179	61,071
Payments on redemption of redeemable units	(18,657)	-
	483,522	61,071
Net increase in cash	44	-
Effect of exchange rate changes on cash	(44)	-
Cash, beginning and end of year	**$ -**	**$ -**

See accompanying Notes to the Financial Statements.

US MORTGAGE OPPORTUNITY FUND

Schedule of Investments
as at December 31
(all amounts in thousands)

	2018		2017	
	Fair Value	**Cost**	**Fair Value**	**Cost**
Mortgage Investments [1]**:**	$ 132,893	$ 116,647	$ 60,653	$ 60,259
Loans (note 4)	440,260	427,240	-	-
Money Market Investments:				
Units in BCI Pooled Investment Portfolio:				
Fund ST1	7	7	102	102
Fund ST3	3,462	3,461	-	-
	3,469	3,468	102	102
Total Investments	$ 576,622	$ 547,355	$ 60,755	$ 60,361

[1] The mortgage investments are held through a private corporation and a trust.

See accompanying Notes to the Financial Statements.

US MORTGAGE OPPORTUNITY FUND

Financial Risk Management Discussion
as at December 31

The investment objectives, eligible investments and general information on the financial risks related to the US Mortgage Opportunity Fund are described in note 7 of the financial statements. The information contained in this Financial Risk Management Discussion pertains specifically to the US Mortgage Opportunity Fund.

The Fund holds its mortgage investments through a private corporation and a trust and its related party loans directly. The Fund, corporation and trust hold the following underlying net assets and direct loans:

(in 000s)	2018 Total	2018 % of Total	2017 Total	2017 % of Total
Unlisted Mortgage Investee Fund	$ 129,340	22.6 %	$ 60,586	99.9 %
BCI Money Market Fund	3,553	0.6 %	67	0.1 %
Loans	440,260	76.8 %	-	- %
	$ 573,153	100.0 %	$ 60,653	100.0 %

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 corporation and trust and their investing activities have been considered.

Credit Risk

The Fund has indirect exposure to credit risk through its investment in shares of an unlisted mortgage investee fund, whose underlying investments are susceptible to credit risk. Such indirect exposure is managed by the external manager in conjunction with investment level decisions.

The Fund's loans were made to a closely held private company which is a related party as described in note 4. Due to the private nature of the loans, they are not subject to rating by a rating agency. The maximum credit risk exposure is $440,260,000 CAD (2017 - $nil).

Financial Risk Management Discussion (continued)
as at December 31

Liquidity Risk

The Fund's financial assets include an unlisted mortgage investee fund and loans, which are generally illiquid. As a result, the Fund may not be able to liquidate its investment in these instruments in due time to meet its obligations when they become due. However, the Chief Investment Officer may obtain funding from unitholders of the Fund through additional unit issuances to meet the Fund's ongoing liquidity requirements.

The Fund's liabilities are due within three months of the year-end of the Fund.

Interest Rate Risk

The Fund is not subject to significant amounts of risk due to fluctuations in the prevailing market interest rates. The Fund has indirect exposure to interest rate risk through its investment in shares of an unlisted mortgage investee fund, whose underlying investments are susceptible to interest rate risk. Such indirect exposure is managed by the external manager in conjunction with their investment level decisions.

At December 31, the Fund has loans oustanding to a borrower whose underlying investments are variable rate mortgage investments. As a result, the Fund's loans do not have significant exposure to interest rate risk.

Currency Risk

The Fund holds net financial assets denominated in U.S. currency totalling $597,871,000 CAD which represents 100.1% of the net asset value of the Fund (2017 - $60,586,000 CAD which represented 99.8% of the net asset value of the Fund). As at December 31, if the Canadian dollar had strengthened/weakened by 1 percent in relation to all other currencies, holding all other variables constant, net assets would have decreased/ increased, respectively, by $5,979,000 CAD (2017 - $606,000 CAD), representing 1.0% of the Fund's net assets (2017 – 1.0%). In practice, the actual trading results may differ from the above sensitivity analysis and the difference could be material.

US MORTGAGE OPPORTUNITY FUND

Financial Risk Management Discussion (continued)
as at December 31

Currency Risk (continued)

As at December 31, the Fund had additional exposure to currency risk through its future unfunded commitments in U.S. currency totalling $1,392,831,000 CAD (2017 - $186,027,000 CAD). As at December 31, if the Canadian dollar had strengthened/weakened by 1 percent in relation to all other currencies, holding all other variables constant, future unfunded commitments would have decreased/increased, respectively, by $13,928,300 CAD (2017 - $1,860,000 CAD). In practice, the actual trading results may differ from this sensitivity analysis and the difference could be material.

Total unfunded committed capital related to the Fund is described in note 6 of the financial statements

Other Price Risk

As at December 31, the Fund made loans to a private company and held an investment in one unlisted mortgage investee fund. The underlying mortgage investee fund is concentrated solely in the United States.

As at December 31, had the fair value of the mortgage investee fund and the loans increased or decreased by 10% with all other variables held constant, net assets attributable to holders of redeemable units would have increased or decreased, respectvely, by approximately $56,960,000 (2017 - $6,059,000) or 10.0% (2017 - 10.0%) of net assets attributable to holders of redeemable units. Actual trading results may differ from the above sensitivity analysis and the difference could be material.

Fair Value Measurement Discussion
as at December 31

Fair Value Hierarchy

As described in note 8 of the financial statements, a three-tier hierarchy is used as a framework for disclosing fair value based on inputs used to value the Fund's financial instruments.

The tables below analyze financial instruments measured at fair value at the reporting date by the level in the fair value hierarchy into which the fair value measurement is categorized. The amounts are based on the values recognized in the Statement of Financial Position. All fair value measurements below are recurring.

	2018			
(in 000s)	Level 1 (Quoted Price in Active Market)	Level 2 (Significant Observable Inputs)	Level 3 (Significant Unobservable Inputs)	Total
BCI Money Market Fund	$ 7,022	$ -	$ -	$ 7,022
Loans	-	269,475	170,785	440,260
Unlisted Mortgage Investee Fund	-	-	129,340	129,340
Total Investments	$ 7,022	$ 269,475	$ 300,125	$ 576,622

	2017			
(in 000s)	Level 1 (Quoted Price in Active Market)	Level 2 (Significant Observable Inputs)	Level 3 (Significant Unobservable Inputs)	Total
BCI Money Market Fund	$ 169	$ -	$ -	$ 169
Unlisted Mortgage Investee Fund	-	-	60,586	60,586
Total Investments	$ 169	$ -	$ 60,586	$ 60,755

During 2018, there were no significant transfers between Level 1 and Level 2.

US MORTGAGE OPPORTUNITY FUND

Fair Value Measurement Discussion (continued)
as at December 31

Fair Value Hierarchy (continued)

The carrying amount of the Fund's net assets attributable to holders of redeemable units also approximates fair value as they are measured at redemption amount and are classified as Level 2 in the fair value hierarchy.

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

	2018		
(in 000s)	Unlisted Private Equity Investee Funds	Loan	Total
Balance, beginning of year	$ 60,586	$ -	$ 60,586
Total gains or (losses) recognized in profit or loss	5,834	(8,704)	(2,870)
Purchases	122,057	179,489	301,546
Sales	(59,137)	-	(59,137)
Balance, end of year	$ 129,340	$ 170,785	$ 300,125
Total unrealized gains or (losses) for the year included in profit or loss relating to financial assets and liabilities held at the reporting date	$ 3,990	$ (8,704)	$ (4,714)

Fair Value Measurement Discussion (continued)
as at December 31

Fair Value Hierarchy (continued)

	2017	
(in 000s)	Unlisted Private Equity Investee Funds	Total
Balance, beginning of year	$ -	$ -
Total gains recognized in profit or loss	1,449	1,449
Purchases	59,137	59,137
Balance, end of year	$ 60,586	$ 60,586
Total unrealized gains for the year included in profit or loss relating to financial assets and liabilities held at the reporting date	$ 1,449	$ 1,449

During 2018, there were no significant transfers into or out of Level 3.

US MORTGAGE OPPORTUNITY FUND

Fair Value Measurement Discussion (continued)
as at December 31

Significant Unobservable Inputs Used in Measuring Fair Value

The table below sets out information about significant unobservable inputs used at year-end in measuring the fair value of the Fund's loans and unlisted mortgage investee funds categorized as Level 3 in the fair value hierarchy as at December 31:

2018

	Fair Value (in 000s)	Valuation Technique	Unobservable Input	Amount / Range	Sensitivity to Change in Significant Unobservable Input
Unlisted Mortgage Investee Fund	$ 129,340	Unadjusted Net Asset Value	Net Asset Value	$ 129,340	The estimated fair value would increase (decrease) if the net asset value of the unlisted mortgage investee fund was higher (lower).
Loan	$ 170,785	Residual value	Residual value	$ 170,785	The estimated fair value would increase (decrease) if the residual value of an internally managed investment entity was higher (lower).

2017

	Fair Value (in 000s)	Valuation Technique	Unobservable Input	Amount / Range	Sensitivity to Change in Significant Unobservable Input
Unlisted Mortgage Investee Fund	$ 60,586	Unadjusted Net Asset Value	Net Asset Value	$ 60,586	The estimated fair value would increase (decrease) if the net asset value of the unlisted mortgage investee fund was higher (lower).

Fair Value Measurement Discussion (continued)
as at December 31

Significant Unobservable Inputs Used in Measuring Fair Value (continued)

Significant unobservable inputs are developed as follows:

(i) Net Asset Value:

Represents the net asset value of the unlisted mortgage investee fund. BCI management values this fund primarily based on the latest available financial information provided by the general partner.

The unlisted mortgage investee fund is subject to redemption restrictions and accordingly the Fund is unable to dispose of the investee until the maturity or wind up and liquidation of the respective investee. In such cases, it is the Fund's policy to categorize the investee as level 3 within the fair value hierarchy.

(ii) Residual value:

Represents the residual value of an internally managed investment entity which is calculated based on the fair value of mortgage investments held by the investment entity, adjusted for the investment entity's working capital and the fair value of the variable rate loan from the Fund to the investment entity (note 4).

US MORTGAGE OPPORTUNITY FUND

Fair Value Measurement Discussion (continued)
as at December 31

Effects of Unobservable Inputs on Fair Value Measurement

The unlisted mortgage investee fund is valued based on information received from the external manager through a co-investment arrangement. The fair value of this investment fluctuates in response to changes in specific assumptions for that particular investee as determined by the external manager.

BCI management estimates the fair market value of the Fund's loans. The fair value of these investments fluctuates in response to changes in specific assumptions for the key unobservable inputs.

Although the Fund believes that 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 the holders of redeemable units.

The following table shows how the net assets attributable to holders of redeemable units would change if the valuations of the unlisted mortgage investee fund and loan investments were calculated by adjusting the respective other mortgage investments' net assets by 10%.

(in 000s)	2018	2017
Favourable	$ 30,013	$ 6,058
Unfavourable	$ (30,013)	$ (6,058)

Involvement with Structured Entities
as at December 31

The Fund's investments are held primarily through one intermediary holding corporation and a trust, 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 legal, tax and other risks that may arise in the course of administering the underlying investments. The carrying amount of these entities of approximately $132,893,000 (2017 - $60,653,000) is shown under Investments in the Statement of Financial Position.

In addition, the Fund holds interests in other structured entities, both directly and indirectly (i.e. through the intermediary holding corporations). The other structured entities are comprised of directly held investee money market funds organized as unit trusts. The tables below set out the direct and indirect interests held by the Fund in these other structured entities:

	December 31, 2018		
Entity	Number of Investee Funds	Total Net Assets of Investee Funds (in 000s)	Carrying Amount Included in Investments in the Statement of Financial Position (in 000s)
Investee money market fund administered by BCI	2	$ 2,522,000	$ 7,022
Unlisted mortgage investments investee fund administered by third party managers	1	$ 625,869,000	$ 129,340

US MORTGAGE OPPORTUNITY FUND

Involvement with Structured Entities (continued)
as at December 31

	December 31, 2017		
Entity	Number of Investee Funds	Total Net Assets of Investee Funds (in 000s)	Carrying Amount Included in Investments in the Statement of Financial Position (in 000s)
Investee money market fund administered by BCI	1	$ 923,071	$ 169
Unlisted mortgage investments investee funds administered by third party managers	1	$ 289,943	$ 60,586

The carrying amount of the investments held in these underlying funds represents the Fund's maximum exposure to loss. During 2018 the Fund did not provide financial support to these structured entities and has no intention of providing financial or other support.

1. The Portfolios

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 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 (the "Regulations"), 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 (the Funds) previously established under the *Financial Administration Act* and the *Pooled Investment Portfolios Regulation*, 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 Funds were established on the following dates:

Pooled Investment Portfolios	Dates Established
Mezzanine Mortgage Fund	September 28, 1999
US Mortgage Opportunity Fund	August 10, 2016

2. Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in compliance with International Financial Reporting Standards (“IFRS”). These financial statements were authorized for issue by the Chief Executive Officer / Chief Investment Officer on July 4, 2019.

(b) Accounting for investments

The Funds qualify as investment entities as they meet 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 Funds meet the definition of an investment entity as defined in IFRS 10.

(c) Basis of measurement

These financial statements have been prepared on a historical cost basis except for investments, which are measured at fair value.

2. Basis of preparation (continued)

(d) Functional and presentation currency

These financial statements are presented in Canadian dollars which is the Funds' 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, BCI 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 necesssarily 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. This information relates 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: amortized cost, fair value through other comprehensive income ("FVOCI") or fair value through profit or loss ("FVTPL"). 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 FVTPL in which case transaction costs are expensed as incurred.

Financial assets and financial liabilities are recognized initially on the trade date, which is the date on which the Funds become a party to the contractual provisions of the instrument. The Funds derecognize a financial liability when its contractual obligations are discharged, cancelled or expire.

3. Significant accounting policies (continued)

(a) Financial instruments (continued)

(i) Recognition and measurement (continued)

Financial assets and liabilities are offset and the net amount presented in the Statement of Financial Position only when the Funds have 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.

A financial asset is measured at amortized cost if it meets both of the following conditions:
- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A financial asset is measured at FVOCI if it meets both of the following conditions:
- it is held within a business model whose objective is to hold assets to collect contractual cash flows and sell financial assets; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

All financial assets not classified as measured at amortized cost or FVOCI as described above are measured at FVTPL. On initial recognition the Funds irrevocably elect to measure financial assets that otherwise meets the requirements to be measured at amortized cost or at FVOCI as at FVTPL when doing so results in more relevant information.

Financial assets are not reclassified subsequent to their initial recognition, unless the Funds change their business model for managing financial assets, in which case all affected financial assets are reclassified on the first day of the first reporting period following the change in the business model.

The Funds have not classified any of its financial assets as FVOCI.

A financial liability is generally measured at amortized cost, with exceptions that may allow for classification as FVTPL. These exceptions include financial liabilities that are mandatorily measured at fair value through profit or loss, such as derivative financial liabilities. On initial recognition the Funds irrevocably designate a financial liability as measured at FVTPL when doing so results in more relevant information.

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 in the period in which they occur. The Funds' investments and redeemable units are classified 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 derivatives and marketable securities) are based on quoted market prices at the close of trading on the reporting date. The Funds' 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 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. Should the value of the financial asset or liability, in the opinion of BCI, be inaccurate, unreliable or not readily available, the fair value is estimated on the basis of the most recently reported information of a similar financial asset or liability.

(iii) Amortized Cost

Financial assets and liabilities classified as amortized cost are recognized initially at fair value plus any directly attributable transaction costs. Subsequent measurement is at amortized cost using the effective interest method, less any impairment losses. The Funds classify other accounts receivable, BCI cost recoveries payable, and other accounts payable as amortized cost.

The effective interest method is a method of calculating the amortized cost of a financial asset or liability and of allocating interest income or expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments through the expected life of the financial asset or liability, or where appropriate, a shorter period.

(b) Redeemable units

The Funds classify 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, each Fund is required to distribute, to unitholders of the respective 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. Distributions to holders of redeemable units are recognized in comprehensive income when they are authorized and no longer at the discretion of BCI.

3. Significant accounting policies (continued)

(c) Issue and redemption of units

Participation in each Fund is expressed in units. The initial value of a unit on inception is $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 one Fund invests in another 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. The US Mortgage Opportunity Fund is an open participation Fund that opens the first business day of the year. The number of units available for issue was unlimited and the proportion of units issued or redeemed by each client on the Fund opening date depended on changes to their desired asset allocation. The Mezzanine Mortgage Fund is a fixed participation fund where participation is fixed for the life of the fund.

(d) Revenue 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. Pursuit costs are charged to net income of the respective Funds in the period incurred.

(e) Income taxes

The Funds qualify as inter-vivos trusts under section 108(1) of the *Income Tax Act (Canada)*. All of the Funds' 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 Funds. As a result, the Funds do not record income taxes. Income taxes associated with any of the Funds’ underlying investments are accounted for in determining the fair value of the respective investments.

3. Significant accounting policies (continued)

(f) Change in accounting policy:

The Funds have adopted IFRS 9 *Financial Instruments* ("IFRS 9") with a date of initial application of January 1, 2018. The requirements of IFRS 9 represent a significant change from IAS 39 *Financial Instruments: Recognition and Measurement* ("IAS 39"). IFRS 9 specifies the accounting for financial instruments, including: classification and measurement, impairment, and hedge accounting. The adoption of IFRS 9 has been applied retrospectively. The nature and effects of the key changes to the Funds' accounting policy are summarized below.

(i) Classification and measurement of financial assets and liabilities:

IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost, FVOCI and FVTPL. The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. The Fund may also, at initial recognition, irrevocably designate a financial asset as measured at FVTPL when doing so results in more relevant information. IFRS 9 eliminates the previous IAS 39 categories of held to maturity, loans and receivables and available-for-sale.

A financial liability is generally measured at amortized cost, with exceptions that may allow for classification as FVTPL. These exceptions include financial liabilities that are mandatorily measured at fair value through profit or loss, such as derivatives liabilities. The Fund may also, at initial recognition, irrevocably designate a financial liability as measured at FVTPL when doing so results in more relevant information.

The adoption of IFRS 9 did not result in any measurement or classification differences in the Funds' financial assets and liabilities as at the transition date. The following table shows the original classification and measurement categories under IAS 39 and the new classification and measurement categories under IFRS 9 for each class of the Funds' financial assets and financial liabilities as at January 1, 2018.

	Original Classification under IAS 39	New Classification under IFRS 9
Financial assets		
Other accounts receivable	Loans and receivables	Amortized cost
Investments	FVTPL	FVTPL
Financial liabilities		
BCI cost recoveries payable	Other financial liabilities	Amoritized cost
Other accounts payable	Other financial liabilities	Amoritized cost
Redeemable units	FVTPL	FVTPL

3. Significant accounting policies (continued)

(f) Change in accounting policy (continued):

(ii) Impairment of financial assets:
IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. As the Funds measure its financial assets at FVTPL and hold only short-term financial assets at amortized cost, the impairment requirements under the new standard do not impact these financial statements.

(iii) Hedge accounting
As permitted by IFRS 9, an election is available to continue to apply the hedge accounting requirements of IAS 39. However, the Funds have not applied hedge accounting under either standard. Therefore, the hedge accounting requirements under the new standard do not impact these financial statements.

(g) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations as listed below are not yet effective for the year ended December 31, 2018, and have not been applied in preparing these financial statements. None of these will have a significant effect on the financial statements of the Funds.

Effective on January 1, 2019:

- IFRS 16 Leases
- IFRIC 23 Uncertainty over Tax Treatments
- Prepayment Features with Negative Compensation (Amendments to IFRS 9)
- Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)
- Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)
- Annual Improvements to IFRS Standards 2015-2017 Cycle - various standards

Effective on January 1, 2020:

- Amendments to References to Conceptual Framework in IFRS Standards

Effective on January 1, 2021:

- IFRS 17 Insurance Contracts

4. Related party transactions

(a) BCI cost recoveries

Third party costs that are attributable to a specific Fund are charged to that Fund. Other costs initially borne by BCI are recovered from the various Funds. BCI cost recoveries and the corresponding payable are disclosed in each Fund's statement of comprehensive income and statement of financial position, respectively.

(b) Related party loans

In March 2018, the US Opportunity Mortgage Fund extended credit to Jutland Finance Inc. in the form of two revolving loans – one variable rate loan in the aggregate principal amount of $2,580,000,000 and one participating loan in the aggregate principal amount of $1,720,000,000 for the purpose of financing the origination and acquisition by Jutland Finance Inc. of U.S. mortgage secured loan investments. Jutland Finance Inc. is wholly owned by British Columbia Investment Management Corporation, the trustee of the Fund. The interest on the variable rate loan is based on LIBOR plus 3.75% and the interest on the participating loan is based on the lesser of 95% of the net profit of Jutland Finance Inc. over the average outstanding principal amount of the loan during the interest period or 12% per annum. The terms in these loans reflect fair market value based on an arms' length transaction.

5. Redeemable units

The Funds are authorized to issue an unlimited number of units. Units issued and outstanding represent the capital of each Fund. The Funds are not subject to any internally or externally imposed restrictions on their capital. BCI manages the capital of each Fund in accordance with the respective 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 ended:

	MEZZANINE MORTGAGE FUND		**US MORTGAGE OPPORTUNITY FUND**	
	2018	**2017**	**2018**	**2017**
Outstanding, beginning of year	39.543	40.208	2,816.449	0.010
Issued for cash	1.691	3.220	22,880.191	2,816.439
Issued on reinvestment of distributions	5.951	0.909	76.260	-
Consolidation of units	(5.951)	(0.909)	(76.260)	-
Redeemed	(18.651)	(3.885)	(834.587)	-
Outstanding, end of year	22.583	39.543	24,862.053	2,816.449

6. Unfunded committed capital

Unfunded capital commitments represent total commitments minus net contributions outstanding as of the reporting date. Net contributions equals contributions less any recallable capital distributions. Recallable capital are distributions or previously contributed capital that has been returned, that may be recalled at some future date. Thus, due to changes in recallable capital, unfunded commitments may change at different reporting dates.

Furthermore, commitments to unlisted mortgage investee funds and direct private debt investments are typically made in US dollars or Canadian dollars, but reported in Canadian dollars. Unfunded commitments are translated at the spot rate and net contributions are translated at historical exchange rates. Therefore, due to foreign exchange movements, unfunded commitments will vary on the reporting date.

The amounts in the table represent the contractual undiscounted cash commitments that can be called on demand.

Pooled Investment Portfolios (in $000s)	Unfunded committed capital	
	As of December 31, 2018	As of December 31, 2017
Mezzanine Mortgage Fund	74,728	81,017
US Mortgage Opportunity Fund	1,392,831	186,027

7. Financial risk management

(a) Risk management framework

Each Fund has its own investment objectives. The Funds' overall risk management program seeks to minimize the potentially adverse effect of risk on the Funds' financial performance in a manner consistent with the Funds' investment objectives. In the normal course of business, each Fund is exposed to financial risks including credit risk, liquidity risk, and market risk (including interest rate risk, currency risk and other price risk). The level of risk varies depending on the investment objective of the Fund and the type of investments it holds. The mandates and investment policies are described below.

Mezzanine Mortgage Fund

The Mezzanine Mortgage Fund invests in highly levered real estate loans that provide investors with higher returns to compensate for the increased risks. These mortgages may provide fixed term or construction financing for multi-family residences (e.g. apartments, condominiums, and seniors' developments), office, retail and industrial buildings. The Fund does not provide mortgages for single-family homes. The Fund maintains a prudent level of diversification. The additional risks associated with construction projects are mitigated by requiring the involvement of only experienced developers, obtaining construction engineer evaluations, requiring significant pre-sales/pre-leasing levels and sufficient profit margin levels, as well as obtaining additional security provisions from borrowers. The performance benchmark for the Mezzanine Mortgage Fund is the FTSE Canada 365 Day T-Bill Index plus 410 basis points.

The Fund invests in the following securities:

- Canadian first, second or third mortgages, or equity participation investments, on commercial property or raw land,
- Units/shares in Canadian mortgage trusts, mortgage funds, limited partnerships, co-investment agreements, and parallel investments agreements, where the underlying assets comply with these investment policies,
- A/B Notes, providing noteholders with a pro rata interest in a first mortgage loan or loans, with the security in favour of holders of B Notes subordinated to the security in favour of corresponding A Notes,
- BCI Canadian Money Market Funds (ST1) and (ST2), and
- Units in BCI's Floating Rate Funds.

7. Financial risk management (continued)

(a) Risk management framework (continued)

US Mortgage Opportunity Fund

The US Mortgage Opportunity Fund is an open participation pool consisting of higher risk real estate loans that provide investors with higher returns to compensate for the increased risks. These mortgages may provide fixed term or construction financing for multi-family residences, office, retail, hospitality, industrial buildings and land development. The Fund does not provide mortgages for single-family homes, however it may provide financing on single-family land subdivisions. The Fund maintains a prudent level of diversification. The additional risks associated with construction projects are mitigated by requiring the involvement of only experienced developers, obtaining construction engineer evaluations, requiring significant pre-sales/pre-leasing levels and sufficient profit margin levels, as well as, obtaining additional security provisions from borrowers where applicable. The performance benchmark for the US Mortgage Opportunity Fund is the Bank of America Merrill Lynch US Treasuries (1-10 Year) Index + 200 basis points .

The Fund invests in the following securities:

- US first, second and third mortgages, structured financing, and/or equity participation investments, on properties or raw land,
- Directly or indirectly, units/shares in US mortgage trusts, mortgage funds, limited partnerships, co-investment agreements, and parallel investment agreements where the underlying assets comply with these investment policies,
- Units in pooled funds of external managers provided such holdings are permissible investments for the Pool, and
- Units in BCI's US Dollar Money Market Fund (ST3) and other BCI short-term fixed income pooled funds for cash management purposes.

7. Financial risk management (continued)

(b) Credit risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Funds, resulting in a financial loss to the Funds. It arises principally from debt securities held, cash and other receivables due to the Funds. The carrying value of these financial instruments as recorded in the Statements of Financial Position reflects the Funds' maximum exposure to credit risk.

To avoid undue credit risk, BCI management has established specific investment criteria, such as minimum credit ratings for investees and counterparties. Counterparty risk represents the credit risk from current potential and future exposure related to transactions. In order to minimize counterparty risk, counterparties are required to provide adequate collateral and meet minimum credit rating requirements. BCI management frequently monitors the credit rating of its counterparties as determined by credit rating agencies and assesses mortage investments for impairment, including significant changes in credit risk.

The Funds' activities may also give rise to settlement risk. Settlement risk is the risk of loss due to failure of an entity to honour its obligations to deliver cash, securities, or other assets prior to the settlement of the transaction as contractually agreed. All investment transactions are settled or paid upon delivery with approved brokers. The risk of default is mitigated since the delivery of securities sold is made simultaneously with the broker receiving payment. Payment is made on a purchase once the securities have been received by the broker. The trade fails if either party fails to meet its obligations.

See additional discussion of credit risk in the Financial Risk Management Discussion in the notes specific to each Fund.

(c) Liquidity risk

Liquidity risk is the risk that the Funds will encounter difficulty in meeting the obligations associated with their financial liabilities that are settled by delivering cash or another financial asset. BCI's approach to managing liquidity risk is to ensure, as far as possible, that each Fund has sufficient liquidity to meet its liabilities when due. Each Fund is exposed to the liquidity risk associated with the requirement to redeem units. Units of the Funds may only be acquired by eligible clients or client groups in accordance with the respective 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 each Fund. The purchase and redemption limits may vary depending on market circumstances, client demand, and the liquidity of the underlying investments.

The Funds' cash position is monitored on a daily basis. In general, investments in cash and BCI Money Market Funds are expected to be highly liquid. BCI management utilizes appropriate measures and controls to monitor liquidity risk in order to ensure that there is sufficient liquidity to meet financial obligations as they come due. The Funds' liquidity position is monitored daily by taking into consideration future forecasted cash flows. This attempts to ensure that sufficient cash reserves are available to meet forecasted cash outflows.

See additional discussion of liquidity risk in the Financial Risk Management Discussion in the notes specific to each Fund.

7. Financial risk management (continued

(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 Funds' income or the fair value of their holdings of financial instruments. Each Fund's strategy for the management of market risk is driven by the Fund's investment objective.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of financial instruments will fluctuate as a result of changes in market interest rates.

The money market investments, and mortgages are subject to interest rate risk. The Funds have established duration bands based on their relevant benchmarks to avoid undue active interest rate risk. Money market funds invest in short-term investments and have low interest rate risk.

See additional discussion of interest rate risk in the Financial Risk Management Discussion in the notes specific to each Fund.

(ii) Other price risk

Other price risk is the risk that the fair value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate risk or currency risk), whether caused by factors specific to an individual investment or its issuer or factors affecting all instruments traded in the market.

All financial instruments are subject to other price risk and a potential loss of capital. The maximum risk is determined by the market value of the financial instruments. There are established investment criteria for each Fund related to diversification of investments and investment mandates for external managers to avoid undue market risk.

See additional discussion of other price risk in the Financial Risk Management Discussion in the notes specific to each Fund.

8. Fair value of financial instruments

(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 Funds determine 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 measure fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

Level 1 inputs that are quoted market prices (unadjusted) in active markets for identical instruments.
Level 2 inputs other than quoted prices included within Level 1 that are observable either directly (i.e., as prices) or indirectly (i.e., derived from prices).
Level 3 inputs that are unobservable.

See additional discussion on the three-tier hierarchy in the Fair Value Measurement Discussion in the notes specific to each Fund.

(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 Funds use widely recognized valuation methods for determining the fair value of common and more simple financial instruments such as foreign currency contracts and 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 exists 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, money market prices, and foreign currency exchange rates in estimating valuations of foreign currency contracts.

Observable prices and model inputs are usually available in the market for listed debt and equity securities, exchange-traded derivatives and simple OTC derivatives. 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.

8. Fair value of financial instruments (continued)

(c) Valuation framework

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

- verifying that the broker or pricing service is approved by the Funds 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.

(d) Financial instruments not measured at fair value

The carrying value of other accounts receivable, BCI cost recoveries payable, and other accounts payable approximates their fair value given their short-term nature. These financial instruments are classified as Level 2 in the fair value hierarchy because while prices are available, there is no active market for these instruments.

9. Taxes

Net cumulative capital losses and non-capital losses for each Fund having such losses are as follows:

Pooled Investment Portfolios (in $000s)	**As of December 31, 2018**	
	Net Capital Losses	**Non-capital Losses**
Mezzanine Mortgage Fund	1	-

Net capital losses are available to be carried forward indefinitely and applied against future net realized capital gains. Non-capital losses may be carried forward up to 20 years to reduce future taxable income.

10. Subsequent event

Effective April 1, 2019, the administration of BCI’s mortgage program transitioned to QuadReal Property Group LP, a subsidiary of a Fund managed by BCI.