Canadian Air Transport Security Authority | Administration canadienne de la sûreté du transport aérien

Quarterly Financial Report

For the Three Months Ended
June 30, 2019

Canada

CATSA ACSTA

CANADIAN AIR TRANSPORT SECURITY AUTHORITY
MANAGEMENT'S NARRATIVE DISCUSSION
FOR THE THREE MONTHS ENDED JUNE 30, 2019

Management's Narrative Discussion outlines the significant activities and initiatives, risks and financial results of the Canadian Air Transport Security Authority (CATSA) for the three months ended June 30, 2019. This Narrative Discussion should be read in conjunction with CATSA's unaudited condensed interim financial statements for the three months ended June 30, 2019, which have been prepared in accordance with Section 131.1 of the *Financial Administration Act* (FAA) and International Accounting Standard 34 *Interim Financial Reporting* (IAS 34). This Narrative Discussion should also be read in conjunction with CATSA's *2019 Annual Report*. At the time of publishing, CATSA's *2019 Annual Report* has not been tabled in Parliament. Until that time, CATSA is not in a position to provide the Management Discussion and Analysis for the year ended March 31, 2019. As a result, certain supplemental information has been provided in this Narrative Discussion. The information in this report is expressed in thousands of Canadian dollars and is current to August 23, 2019, unless otherwise stated.

Forward-looking statements

Readers are cautioned that this report includes certain forward-looking information and statements. These forward-looking statements contain information that is generally stated to be anticipated, expected or projected by CATSA. They involve known and unknown risks, uncertainties and other factors which may cause the actual results and performance of the organization to be materially different from any future results and performance expressed or implied by such forward-looking information.

Materiality

In assessing what information is to be provided in this report, management applies the materiality principle as guidance for disclosure. Management considers information material if it is probable that its omission or misstatement, judged in the surrounding circumstances, would influence the economic decisions of CATSA's stakeholders.

CORPORATE OVERVIEW

CATSA is an agent Crown corporation, funded by parliamentary appropriations and accountable to Parliament through the Minister of Transport. CATSA's mission is to protect the public by securing critical elements of the air transportation system.

CATSA delivers the mandate of security screening at 89 designated airports across the country through a third-party screening contractor model. CATSA is responsible for the delivery of the following four mandated activities:

- Pre-Board Screening (PBS): the screening of passengers, their carry-on baggage and their belongings prior to their entry to the secure area of an air terminal building;
- Hold Baggage Screening (HBS): the screening of passengers' checked (or hold) baggage for prohibited items, prior to being loaded onto an aircraft;
- Non-Passenger Screening (NPS): the random screening of non-passengers and their belongings, including vehicles, entering restricted areas of the aerodrome at the highest risk airports; and

- Restricted Area Identity Card (RAIC) Program: the system which uses iris and fingerprint biometric identifiers to allow non-passengers access to the restricted areas of airports.

CATSA is also responsible for ensuring consistency in the delivery of screening across Canada and for air transport security functions that the Minister of Transport may assign to it, subject to any terms and conditions that the Minister may establish.

In addition to its mandated activities, CATSA has an agreement with Transport Canada (TC) to conduct screening of cargo at smaller airports where capacity exists. This program was designed to screen limited amounts of cargo during off-peak periods and involves using existing resources, technology and procedures.

With the support of TC, CATSA entered into a Supplemental Screening Services agreement to trial cost recovery at PBS with the Greater Toronto Airports Authority (GTAA) for the provision of supplemental screening services effective October 5, 2014, and extended annually thereafter. CATSA also entered into a similar agreement with the Vancouver International Airport Authority (YVRAA) effective June 26, 2017. The YVRAA trial agreement ended June 30, 2018. CATSA received approval from TC to extend the ongoing agreement with GTAA until March 31, 2020.

CATSA also entered into an agreement with the Muskoka Airport Authority to provide screening services over a 10-week period. Approval was obtained from TC and the 10-week period began in June 2019.

2018/19 ANNUAL HIGHLIGHTS

- As always, CATSA's various teams of highly qualified experts worked together to ensure the delivery of screening services across Canada was effective, efficient, consistent and professional.
- In 2018/19, CATSA exceeded its wait time service level target and delivered a wait time service level where, on average, approximately 92% of all passengers waited 15 minutes or less to be screened at Class I airports on an annual basis.
- The *Budget Implementation Act 2019* introduced the *Security Screening Services Commercialization Act,* which enables the creation of a new designated screening authority. The government is targeting to transfer responsibilities from CATSA to a new designated screening authority on April 1, 2020.
- In collaboration with the airport authorities, CATSA continued to deploy the CATSA Plus concept at Vancouver International Airport, Edmonton International Airport, Toronto Pearson International Airport, Montreal-Trudeau International Airport and Halifax Stanfield International Airport.
- A Computed Tomography technology trial was initiated at the Winnipeg James Armstrong Richard International Airport in order to inform the next generation of PBS X-ray equipment.
- The HBS Recapitalization Program continued on track and on budget for completion in 2020/21.
- CATSA continued to work collaboratively and build on its relationships with key national and international stakeholders through a number of initiatives, including the Known Traveller Digital Identity project, and the Canada/U.S. Innovation Task Force and SMART Security.
- In its continued efforts to enhance the customer experience, CATSA participated in a variety of outreach initiatives, including engaging with Indigenous Elders and participating in events targeting community engagement, such as the "I am Pearson" campaign at Toronto Pearson International Airport.
- The average number of passenger complaints was less than one complaint per 50,000 screened passengers in 2018/19.
- Overall passenger satisfaction was at 88%, three points higher than the corporate target of 85%.

OPERATING ENVIRONMENT

ECONOMIC OUTLOOK

Events and developments occurring in the economic environment greatly influence CATSA's operations. Global economic growth slightly increased from 3.6% in 2017 to an estimated 3.7% in 2018. It is expected to slow down to 3.0% in 2019, 3.2% in 2020 and 3.3% in 2021. In Canada, the economy grew by 3.0% in 2017 and 1.9% in 2018 (estimated), while projected to grow by 1.3% in 2019, 1.9% in 2020 and 2.0% in 2021[1].

PASSENGER GROWTH AND SCREENING CONTRACTOR BILLING RATES

Economic growth generally leads to increased passenger travel. Projections indicate that the number of enplaned passengers at Canadian airports will increase by 5.2% in 2019 compared to 2018, and is expected to grow in each of the next 5 years[2].

Passenger traffic forecasts are based on average annual growth across Canada. However, growth does not occur uniformly at all airports. Changes in passenger traffic occur largely on a regional and site-specific basis and without much warning, often as a result of changes in flight schedules or the introduction of new services by air carriers. For CATSA, an increase in passenger traffic can often lead to a higher or sudden demand for screening hours and increased operating expenditures. To support any changes in passenger volumes that may occur, CATSA closely examines its purchases of screening hours among airports. CATSA also works closely with its industry partners on the impact of operational factors, such as flight schedules, available space and passenger arrival patterns, to help manage potential issues related to large influxes of passengers.

Statistics from CATSA's Boarding Pass Security System for the three months ended June 30, 2019, indicate that screened traffic across Canada increased by 1.3% over the same period in 2018, resulting in a need for additional screening hours to maintain wait time service levels.

In addition to passenger growth, screening contractor billing rates will continue to increase annually over the remaining term of the current Airport Screening Services Agreements (ASSAs) that expire on March 31, 2022. This puts further pressure on CATSA's budget for screening hours.

GOVERNMENT FUNDING

CATSA, as an agent Crown corporation, is funded by parliamentary appropriations and accountable to the Parliament of Canada through the Minister of Transport. Consequently, CATSA's financial plan is prepared in accordance with the resources it is assigned by the Government of Canada and as approved by Parliament.

[1] Bank of Canada, *Monetary Policy Report*, January 2019 for year 2017, and Bank of Canada, *Monetary Policy Report*, July 2019 for years 2018, 2019, 2020 and 2021.
[2] SNC Lavalin Inc., February 2019 *Air Passenger Traffic Forecasts for CATSA Designated Airports.*

Budget 2019 included funding of $288.3 million for 2019/20 to continue to protect the public by securing critical elements of the air transportation system. This supplemental funding will allow CATSA to target a wait time service level where, on average, 85% of all passengers are waiting 15 minutes or less to be screened at Class I airports on an annual basis, and to continue to deliver its current enhanced Non-Passenger Screening program. The funding envelope also provides financial resources to support the transfer to the new designated screening authority.

COMPLIANCE WITH DIRECTIVES

In December 2014, the Governor in Council issued a Pension Plan Reform Directive (Order in Council P.C. 2014-1382), pursuant to Section 89 of the *Financial Administration Act* (FAA), directing the Crown Corporations under the Minister of Transport's portfolio, including CATSA, to align with Budget 2013 direction on public sector pension reform. The pension reform included a provision for adjusting the employer/employee current service cost sharing ratio to 50:50 by December 31, 2017.

In July 2015, CATSA received notification that an exemption was available to pension plans that could demonstrate either unfairness to pension plan members, or recruitment and retention challenges, as a result of implementing the pension reform. Following this notification, CATSA began working with its external pension actuary to draft a business case for an exemption on the basis that the pension reform would be unfair to plan members. It is CATSA's view that its business case demonstrates that the closing of the defined benefit pension plan in 2013 would result in an unfair cost sharing burden on employees, and that the cost sharing ratio should be calculated as if the plan were open to new members.

As of January 1, 2018, CATSA aligned its employee contribution rates with the objectives identified in the business case. On June 13, 2019, the Governor in Council issued Order in Council P.C. 2019-783, which, among other things, imposes revised cost sharing principles that are in alignment with CATSA's business case.

NEW ACCOUNTING STANDARD

Effective April 1, 2019, CATSA adopted IFRS 16 *Leases*. IFRS 16 specifies how to recognize, measure, present and disclose leases. This standard introduces significant changes to the lessee accounting by removing the distinction between operating and finance leases and requiring the recognition of a right-of-use asset and lease liability at the lease commencement date for all leases, except for certain leases subject to exemption.

As a result of the new accounting standard, CATSA's Statement of Financial Position now includes the following: right-of-use assets, current lease liabilities, and non-current lease liabilities. The Statement of Comprehensive Income now includes parliamentary appropriations for lease payments to appropriately reflect CATSA's funding for lease payments.

CATSA has applied IFRS 16 using the modified retrospective approach and, accordingly, the prior period information has not been restated. CATSA also elected to record right-of-use assets based on the corresponding lease liability. Refer to note 3 of the financial statements for more information.

RISK ENVIRONMENT

CATSA's ability to respond to an evolving operating and security environment is critical to the organization's success.

Risk management at CATSA is a formalized, systematic approach to determine the best course of action during times of uncertainty by identifying, assessing, evaluating, acting on and communicating risk throughout the organization. This approach contributes to risk-informed decision making, which enables CATSA to effectively manage uncertainties and capitalize on opportunities.

CATSA's risk management program is focused on risks that may impede the organization's ability to meet the following objectives:

- to deliver mandated activities in an effective, efficient and consistent manner, while safeguarding the interests of the travelling public; and
- to provide services or programs in support of its mandated activities.

As a key member of the Canadian civil aviation security system, CATSA is exposed to a variety of risks that may impact the organization's ability to fulfill its mandate. Specific responses to aviation security threats and risks are mandated by TC and implemented by CATSA. In addition to intelligence-related threat information overseen by TC and risk responses, CATSA conducts various risks assessments pertaining to its corporate strategies and operations.

RISK GOVERNANCE

CATSA has established an enterprise risk management framework that identifies corporate risks associated with its operating environment. CATSA conducts an annual corporate risk profiling exercise whereby corporate risks are identified and assessed against established criteria after taking into account the organization's existing controls to mitigate them. Corporate risks are then actively monitored and re-assessed on a quarterly basis by the Senior Management Committee (SMC) and reported to the Board of Directors (BoD). This process is flexible as it enables the organization to include new and emerging risk information for consideration and assessment and enables senior management to analyze emerging and forward-looking risk trends.

Board of Directors

The BoD's key functions and responsibilities are to provide strategic direction, financial oversight, corporate oversight and governance. With respect to risk management, it is accountable for overseeing risk management activities including providing clear direction of risk attitude, and approving the risk management policy as well as the corporate risk profile.

Senior Management Committee

The SMC is responsible for identifying and assessing key risks, evaluating corporate risks as per CATSA's risk attitude and ensuring appropriate controls and mitigation strategies are in place and implemented to effectively manage these risks. The role includes supporting risk awareness and communicating risks throughout the organization.

RISKS AND UNCERTAINTIES

CATSA's key risks are those that could impede the organization's ability to achieve its strategic objectives. The following is a summary of CATSA's key corporate risks identified as at March 31, 2019. There have been no significant changes to the corporate risk profile during the three months ended June 30, 2019.

MANDATED RISK SERVICES

Detection capability

Aviation security is CATSA's top priority. Screening equipment is approved and detection standards are set by TC. While CATSA meets these standards, the organization's detection capability may be limited to the existing technology, processes or human factors. There is a risk that CATSA may not have the technology, the threat and risk information, processes or human factor capability to detect all high-risk threat items, which may result in substantial consequences to the civil aviation system.

To address this risk, CATSA continually works to review, test and improve the effectiveness of its operational processes and procedures, and maintains a capital program to support the replacement and upgrading of screening equipment. CATSA also collaborates regularly with TC to stay apprised of the threat landscape, and utilizes its Threat Detection Baseline tool to identify gaps that need to be addressed, and develop solutions to close these gaps.

CAPACITY RISK

CATSA staff capacity

CATSA's streamlined corporate structure has made the organization leaner, however, at current human resource levels, the organization may face challenges in effectively managing the increasing workload. There is a risk that CATSA's current staff capacity may be inadequate to sustain current workloads and to support a healthy work environment.

To address this risk, the organization monitors current vacancy levels in order to prioritize staffing actions and may use fixed-term resources to alleviate workload pressures in corporate support services.

The decision regarding CATSA's transfer to a new designated screening authority may cause this risk to evolve, as staff continue to manage their current workloads, while also handling any new tasks that arise related to the sale. The organization will monitor this risk closely and adjust, as required.

Level of government funding to deliver core mandate

CATSA's current reference levels have remained flat and the organization has been relying on one-year supplemental funding to fill the funding gap. This impacts the delivery of CATSA's core mandate and the level of service to the travelling public.

Budget 2019 included funding of $288.3 million for 2019/20 to continue to protect the public by securing critical elements of the air transportation system. The supplemental funding will allow CATSA to target a wait time service level where, on average, 85% of all passengers are waiting 15 minutes or less to be screened at Class I airports on an annual basis, and to continue to deliver its current enhanced Non-Passenger Screening program.

Going forward, CATSA's lack of long-term financial resources should be substantially addressed through the enhanced financial and operational flexibility that would be provided with the transfer to a new designated screening authority.

SERVICE DELIVERY THROUGH THIRD-PARTY RISK

Legal or illegal labour disruptions

The majority of the collective bargaining agreements between screening contractors and unions expired on March 31, 2018, and the collective bargaining renewal process is still underway. There is a risk that illegal labour disruptions may occur as a result of union activity and/or CATSA may have limited capacity or resilience to respond to a legal labour disruption event.

To address this risk, CATSA continually monitors labour issues between screening contractors and the unions representing screening officers and keeps TC apprised of developments.

In the event of a legal or illegal labour disruption, CATSA has prepared labour contingency plans with operational, legal and communications components.

Service delivery model – outsourcing of screening services and equipment maintenance services

CATSA is fully dependent on screening contractors for delivering critical and mandated screening services and is primarily dependent on outsourced maintenance service providers for the maintenance of screening equipment. There is a risk that CATSA's business model for outsourced screening services and equipment maintenance may result in service delivery impacts in the event that a contractor is no longer able or willing to provide the agreed-upon services.

To address this risk, CATSA continually monitors screening contractor performance and has developed a screening contractor relationship management framework, which promotes a systematic and collaborative relationship between CATSA and the screening contractors. As well, alternate maintenance arrangements have been put in place to ensure continuity of screening equipment maintenance services.

STAKEHOLDER RELATIONS

Due to a variety of operational issues, there is a risk that CATSA's reputation may be damaged with its stakeholders resulting in loss of public trust or potential increased complaints.

To address this risk, CATSA continues to improve the passenger experience by promoting a customer service-oriented culture. CATSA regularly liaises with industry stakeholders and has implemented a variety of communication strategies such as conducting passenger intercept surveys and the expanded use of social media to engage its multiple stakeholder groups.

COMPLIANCE RISK

Management of sensitive, secret or personal information

CATSA produces, collects and maintains a large amount of sensitive, secret and personal documentation and information. There is a risk that sensitive, secret or personal information in both physical and/or electronic formats across multiple platforms could be lost, stolen or disclosed inappropriately.

To address this risk, CATSA has a variety of physical security and information technology security controls in place and conducts privacy impact assessments for all new or modified programs and activities that involve the use of personal information. CATSA has also established privacy policies and procedures to safeguard the organization against this risk.

HUMAN RESOURCES RISK

Employee recruitment

CATSA endeavours to recruit the best talent available, however, there is a risk that the organization may experience challenges in recruiting key or specialized talent. This may be due to labour market conditions for talent or due to CATSA's overall corporate human resources strategies.

To address this risk, the organization has implemented a number of initiatives to ensure competitive total compensation packages and has expanded its recruitment strategies to include specialized advertising for unique or key talent.

Employee retention

CATSA strives to maintain an engaged, high- performing workforce. There is a risk that CATSA's corporate strategies may impede the organization's ability to retain talent in key and specialized positions.

To address this risk, the organization is focusing on initiatives to retain talent including its talent management and management development programs. The organization has recently implemented a Diversity and Inclusion Framework, which aims to integrate diversity and inclusion values and practices into existing corporate processes.

INFORMATION TECHNOLOGY (IT) RISK

Cyber attacks on IT infrastructure

Government departments, agencies and Crown corporations are constantly exposed to a variety of cyber threats to their IT infrastructure. There is a risk that cyber threats and/or attacks may negatively impact CATSA's IT infrastructure and/or compromise organizationally sensitive information resulting in a loss of public confidence and potential damage to CATSA's reputation.

To address this risk, the organization has a variety of devices, systems, processes and procedures to safeguard the organization's IT infrastructure.

TRANSITION RISK

Seamless Transition

The *Budget Implementation Act* 2019 introduced the *Security Screening Services Commercialization Act*, which enables the creation of a new designated screening authority. As part of CATSA's funding envelope, Budget 2019 provided resources to support TC and CATSA during the transfer to a new designated screening authority.

As CATSA is playing a supporting role in this transition, there is a risk that the organization may not have direct access to the pertinent information required to enable a seamless transition to the new entity by the targeted deadline.

CATSA will address this risk by continuing to pro-actively plan, assess and advise TC on several business impacts related to transition.

ANALYSIS OF FINANCIAL RESULTS

CONDENSED INTERIM STATEMENT OF COMPREHENSIVE INCOME (LOSS)

The following section provides information on key variances within the Condensed Interim Statement of Comprehensive Income (Loss) for the three months ended June 30, 2019, and June 30, 2018.

Key Financial Highlights - Condensed Interim Statement of Comprehensive Income (Loss)	Three Months Ended June 30			
	2019	2018		
(Thousands of Canadian dollars)	(unaudited)	(unaudited)	$ Change	% Change
Expenses[1]				
Screening services and other related costs	$ 151,315	$ 145,132	$ 6,183	4.3%
Equipment operating and maintenance	10,488	9,866	622	6.3%
Program support and corporate services	22,083	21,459	624	2.9%
Depreciation and amortization	17,096	15,320	1,776	11.6%
Total expenses	**200,982**	**191,777**	**9,205**	**4.8%**
Other expenses (income)	**1,466**	**(71)**	**1,537**	**N/M**
Financial performance before revenue and government funding	**202,448**	**191,706**	**10,742**	**5.6%**
Revenue	**4,167**	**4,467**	**(300)**	**(6.7%)**
Government funding				
Parliamentary appropriations for operating expenses	175,864	168,493	7,371	4.4%
Amortization of deferred government funding related to capital expenditures	17,208	15,587	1,621	10.4%
Parliamentary appropriations for lease payments	981	-	981	N/M
Total government funding	**194,053**	**184,080**	**9,973**	**5.4%**
Financial performance	**$ (4,228)**	**$ (3,159)**	**$ (1,069)**	**(33.8%)**
Other comprehensive income (loss)	**(25,074)**	**14,878**	**(39,952)**	**(268.5%)**
Total comprehensive income (loss)	**$ (29,302)**	**$ 11,719**	**$ (41,021)**	**(350.0%)**

[1] The Condensed Interim Statement of Comprehensive Income (Loss) presents operating expenses by program activity, whereas operating expenses above are presented by major expense type, as disclosed in note 13 of the unaudited condensed interim financial statements for the three months ended June 30, 2019.

N/M = not meaningful

Screening services and other related costs

Screening services and other related costs increased by $6,183 (4.3%) for the three months ended June 30, 2019, compared to the same period in 2018. The variance is primarily due to the purchase of additional screening hours totaling $3,642, and annual screening contractor billing rate increases amounting to $3,376.

The increase in screening hours purchased is the result of additional screening requirements to support higher passenger volumes and operational changes at certain airports.

Depreciation and amortization

Depreciation and amortization increased by $1,776 (11.6%) for the three months ended June 30, 2019, compared to the same period in 2018. The increase is primarily due to the adoption of IFRS 16, which requires the depreciation of right-of-use assets in accordance with their respective lease terms. The increase is also due to new HBS equipment deployments as part of the HBS life-cycle management program, as well as new CATSA Plus deployments. The increase is partially offset by older equipment becoming fully depreciated.

Other expenses (income)

Other expenses (income) increased by $1,537 for the three months ended June 30, 2019, compared to the same period in 2018. The increase is mainly due to higher losses on the disposal of property and equipment, as well as losses on the fair value of derivative financial instruments.

Revenue

Revenue decreased by $300 (6.7%) for the three months ended June 30, 2019, compared to the same period in 2018. The decrease is mainly due to the purchase of fewer supplemental screening hours, resulting primarily from the expiry of the trial agreement with YVRAA in June 2018, partially offset by an increase in supplemental screening hours purchased by the GTAA.

Government Funding

CATSA is funded by appropriations from the federal Consolidated Revenue Fund for operating expenses and capital expenditures, which includes funding for lease payments.

Parliamentary appropriations for operating expenses

Parliamentary appropriations for operating expenses increased by $7,371 (4.4%) for the three months ended June 30, 2019, compared to the same period in 2018. The increase is mainly attributable to increased spending for screening services and other related costs, as discussed above.

Amortization of deferred government funding related to capital expenditures

Amortization of deferred government funding related to capital expenditures increased by $1,621 (10.4%) for the three months ended June 30, 2019, compared to the same period in 2018. The increase is mainly attributable to increased depreciation and amortization, excluding depreciation of right-of-use assets, and higher losses on disposal of property and equipment, as previously discussed.

Parliamentary appropriations for lease payments

As a result of the adoption of IFRS 16, the majority of CATSA's lease payments are now funded through capital appropriations, as opposed to parliamentary appropriations for operating expenses. CATSA's lease payments are typically made in the same month that appropriations are received, therefore there is no deferred funding related to these appropriations.

Other comprehensive income (loss)

Other comprehensive income (loss) is composed of quarterly non-cash remeasurements resulting from changes in actuarial assumptions and the return on pension plan assets.

Other comprehensive loss of $25,074 for the three months ended June 30, 2019, is due to a remeasurement loss of $29,796 on the defined benefit liability arising from a 50 basis point decrease in the discount rate since March 31, 2019. This was partially offset by a remeasurement gain of $4,722 resulting from a higher actual rate of return on plan assets than the rate initially used in CATSA's assumptions. Other comprehensive income of $14,878 for the three months ended June 30, 2018, is primarily due to a remeasurement gain of $12,796 on the defined benefit liability arising from a 25 basis point increase in the discount rate between March 31, 2018, and June 30, 2018. It was also due to a remeasurement gain of $2,082 resulting from a higher actual rate of return on plan assets than the rate initially used in CATSA's assumptions

For more information, refer to note 12 of the unaudited condensed interim financial statements.

CONDENSED INTERIM STATEMENT OF FINANCIAL POSITION

The following section provides information on key variances within the Condensed Interim Statement of Financial Position as at June 30, 2019, compared to March 31, 2019.

Key Financial Highlights - Condensed Interim Statement of Financial Position (Thousands of Canadian dollars)	**June 30, 2019** (unaudited)	**March 31, 2019** (audited)	$ Change	% Change
Current assets	$ 173,863	$ 168,550	$ 5,313	3.2%
Non-current assets	500,721	477,009	23,712	5.0%
Total assets	**$ 674,584**	**$ 645,559**	**$ 29,025**	**4.5%**
Current liabilities	$ 170,724	$ 160,710	$ 10,014	6.2%
Non-current liabilities	556,801	508,488	48,313	9.5%
Total liabilities	**$ 727,525**	**$ 669,198**	**$ 58,327**	**8.7%**

Assets

Current assets increased by $5,313 (3.2%) primarily due to the following:

- Increase in cash of $73,693 primarily due to the timing of funds received from the Government of Canada; and
- Decrease in trade and other receivables of $68,064, mainly due to a decrease in parliamentary appropriations receivable.

Non-current assets increased by $23,712 (5.0%) primarily due to the following:

- Increase in right-of-use assets of $24,571 due to the adoption of IFRS 16;
- Increase in property and equipment and intangible assets of $3,665 primarily due to acquisitions totaling $20,915, partially offset by depreciation and amortization of $16,186; and
- Decrease in employee benefits asset of $4,482. The employee benefits asset as at March 31, 2019, was comprised of CATSA's registered pension plan and supplementary retirement plan, which were both in a net asset position. As at June 30, 2019, the registered pension plan is in a net liability position (see explanation in non-current liabilities sections for further detail).

Liabilities

Current liabilities increased by $10,014 (6.2%) primarily due to the following:

- Increase in the current portion of deferred government funding related to capital expenditures of $5,450 primarily due to the timing of funds received from the Government of Canada;
- Increase in current lease liabilities of $3,433 due to the adoption of IFRS 16; and
- Increase in current holdbacks of $1,723 due to ongoing construction under the HBS recapitalization projects.

Non-current liabilities increased by $48,313 (9.5%) primarily due to the following:

- Increase in non-current lease liabilities of $21,675 due to the adoption of IFRS 16;
- Increase in employee benefits liability of $22,736 in relation to CATSA's registered pension plan and other defined benefits plan. The increase in the employee benefits liability is due to the registered pension plan net liability of $17,918 (total variance of $21,849; from a $3,931 asset to a $17,918 liability) and an increase in the other defined benefits plan liability of $4,818. The increases are mainly due to remeasurement losses of $29,245 arising from a 50 basis point decrease in the discount rate used to measure the defined benefit liabilities of these two plans. The increases are also due to defined benefit costs exceeding contributions by $2,131. These increases were partially offset by a remeasurement gain of $4,709 arising from a higher rate of return on plan assets than the rate used in CATSA's assumptions; and
- Increase in the non-current portion of the deferred government funding related to capital expenditures of $3,661 due to capital expenditures funded through parliamentary appropriations of $20,869 exceeding amortization of deferred government funding related to capital expenditures of $17,208.

FINANCIAL PERFORMANCE AGAINST CORPORATE PLAN

CATSA's corporate plan for the current fiscal year has not been tabled for approval in Parliament at the time of publishing. Until it is tabled in Parliament and made publicly available, CATSA will not be in a position to provide an explanation of significant differences between its financial results compared to those anticipated in the corporate plan summary.

PARLIAMENTARY APPROPRIATIONS USED

CATSA's operations are funded primarily by parliamentary appropriations from the Government of Canada. The table below serves to reconcile financial performance reported under International Financial Reporting Standards (IFRS) and operating appropriations used on a near-cash accrual basis:

Reconciliation of Financial Performance to Operating Appropriations Used	Three Months Ended June 30	
	2019	2018
(Thousands of Canadian dollars)	(unaudited)	(unaudited)
Financial performance before revenue and government funding	$ 202,448	$ 191,706
Revenue	(4,167)	(4,467)
Financial performance before government funding	198,281	187,239
Non-cash expenses		
Depreciation and amortization	(17,096)	(15,320)
Employee benefits expense [1]	(2,144)	(2,137)
Employee cost accruals [2]	(1,594)	(1,357)
Loss on disposal of property and equipment	(984)	(52)
Change in fair value of financial instruments at fair value through profit and loss	(637)	114
Finance costs	(128)	-
Write-off of property and equipment	(79)	(250)
Spare parts expense funded from capital [3]	(1)	(4)
Non-cash gain (loss) on foreign exchange recognized in financial performance	246	236
Deferred lease incentives recognized in financial performance [4]	-	24
Parliamentary appropriations for operating expenses	**$ 175,864**	**$ 168,493**
Other items affecting funding		
Net change in prepaid expenses and inventories [5]	(497)	(2,014)
Total operating appropriations used	**$ 175,367**	**$ 166,479**

[1] Employee benefits are accounted for in the Condensed Interim Statement of Comprehensive Income in accordance with IFRS. The reconciling item above represents the difference between cash payments for employee benefits and the accounting expense under IFRS.

[2] Employee cost accruals are accounting adjustments to record variable pay and accrued vacation used and incurred to June 30, 2019. These costs are only recorded for near-cash accrual purposes at year-end, creating a reconciling item during interim periods.

[3] Spare parts expense funded from capital represents items that were funded from capital appropriations in prior years but were used as spare parts and expensed during the current year, creating a reconciling item.

[4] Deferred lease incentives are non-cash accounting adjustments to record the benefit derived from favourable lease terms, including significantly reduced rent, free common area costs and leasehold improvements provided at no cost. Rental costs are funded by appropriations when paid, creating a reconciling item.

[5] Prepaid expenses and inventories are expensed as the benefit is derived from the asset by CATSA. They are funded by appropriations when purchased, creating a reconciling item.

Capital Expenditures

The table below serves to reconcile capital expenditures reported under IFRS and capital appropriations used:

Reconciliation of Capital Expenditures to Capital Appropriations Used	Three Months Ended June 30	
	2019	2018
(Thousands of Canadian dollars)	(unaudited)	(unaudited)
Explosives Detection System	$ 19,819	$ 38,248
Non-Explosives Detection System	1,096	446
Lease Payments	981	-
Total capital expenditures	**$ 21,896**	**$ 38,694**
Non-cash adjustment on foreign exchange related to capital expenditures	(46)	(318)
Proceeds on disposal of property and equipment [1]	-	(21)
Total capital appropriations used	**$ 21,850**	**$ 38,355**

[1] Proceeds on disposal of property and equipment include non-cash proceeds received in the form of credit notes from suppliers.

STATEMENT OF MANAGEMENT RESPONSIBILITY

Management is responsible for the preparation and fair presentation of these unaudited condensed interim financial statements in accordance with International Accounting Standard 34 *Interim Financial Reporting*, and The Treasury Board of Canada *Standard on Quarterly Financial Statements for Crown Corporations* and for such internal controls as management determines are necessary to enable the preparation of the unaudited condensed interim financial statements that are free from material misstatement. Management is also responsible for ensuring all other information in this quarterly financial report is consistent, where appropriate, with the unaudited condensed interim financial statements.

Based on our knowledge, these unaudited condensed interim financial statements present fairly, in all material respects, the financial position, results of operations and cash flows of CATSA, as at the date of and for the periods presented in the unaudited condensed interim financial statements.

Michael Saunders
President and Chief Executive Officer

Ottawa, Canada

August 23, 2019

Nancy Fitchett, CPA, CA
Acting Vice-President, Corporate Affairs and Chief Financial Officer

Ottawa, Canada

August 23, 2019

Condensed Interim Financial Statements of

CANADIAN AIR TRANSPORT SECURITY AUTHORITY

June 30, 2019

(Unaudited)

CANADIAN AIR TRANSPORT SECURITY AUTHORITY

Condensed Interim Statement of Financial Position
(Unaudited)

(In thousands of Canadian dollars)

	June 30, 2019	March 31, 2019
Assets		
Current assets		
Cash	$ 77,700	$ 4,007
Trade and other receivables (note 4)	77,426	145,490
Inventories (note 5)	14,852	15,305
Prepaids	3,885	3,253
Derivative financial assets (note 15)	-	495
	173,863	168,550
Non-current assets		
Property and equipment (note 6)	458,796	455,524
Intangible assets (note 7)	16,108	15,715
Right-of-use assets (note 8)	24,571	-
Employee benefits asset (note 12)	1,246	5,728
Derivative financial assets (note 15)	-	42
	500,721	477,009
Total assets	$ 674,584	$ 645,559
Liabilities and Equity		
Current liabilities		
Trade and other payables	$ 129,524	$ 129,719
Holdbacks	14,156	12,433
Lease liabilities (note 10)	3,433	-
Deferred government funding related to capital expenditures (note 11)	5,450	-
Deferred government funding related to operating expenses (note 11)	18,061	18,558
Derivative financial liabilities (note 15)	100	-
	170,724	160,710
Non-current liabilities		
Holdbacks (note 15)	8,490	7,767
Lease liabilities (note 10)	21,675	-
Deferred lease incentives (note 8)	-	482
Deferred government funding related to capital expenditures (note 11)	473,393	469,732
Employee benefits liability (note 12)	53,243	30,507
	556,801	508,488
Equity		
Accumulated deficit	(52,941)	(23,639)
Total liabilities and equity	$ 674,584	$ 645,559

Contingencies (note 9) and contractual arrangements (note 16)
The accompanying notes are an integral part of these condensed interim financial statements.

CANADIAN AIR TRANSPORT SECURITY AUTHORITY

Condensed Interim Statement of Comprehensive Income (Loss)
(Unaudited)

(In thousands of Canadian dollars)

	Three months ended June 30	
	2019	2018
Expenses		
Pre-Board Screening	$ 112,120	$ 108,854
Hold Baggage Screening	40,895	37,715
Non-Passenger Screening	35,353	33,877
Restricted Area Identity Card Program	772	770
Corporate services	11,842	10,561
Total expenses (note 13)	200,982	191,777
Other expenses (income)		
Loss on disposal of property and equipment	984	52
Net loss (gain) on fair value of derivative financial instruments	637	(114)
Finance costs	129	1
Write-off of property and equipment	79	250
Foreign exchange gain	(363)	(260)
Total other expenses (income)	1,466	(71)
Financial performance before revenue and government funding	202,448	191,706
Revenue		
Screening services - supplemental	3,923	4,279
Finance income	219	188
Screening services - other	25	-
Total revenue	4,167	4,467
Government funding		
Parliamentary appropriations for operating expenses (note 11)	175,864	168,493
Amortization of deferred government funding related to capital expenditures (note 11)	17,208	15,587
Parliamentary appropriations for lease payments (note 14)	981	-
Total government funding	194,053	184,080
Financial performance	$ (4,228)	$ (3,159)
Other comprehensive income (loss)		
Item that will not be reclassified to financial performance		
Remeasurement of defined benefit plans (note 12)	(25,074)	14,878
Total comprehensive income (loss)	$ (29,302)	$ 11,719

The accompanying notes are an integral part of these condensed interim financial statements.

CANADIAN AIR TRANSPORT SECURITY AUTHORITY

Condensed Interim Statement of Changes in Equity
(Unaudited)

(In thousands of Canadian dollars)

For the three months ended June 30:

		Accumulated deficit
Balance, March 31, 2019	$	(23,639)
Financial performance		(4,228)
Item that will not be reclassified to financial performance		
Remeasurement of defined benefit plans (note 12)		(25,074)
Balance, June 30, 2019	$	(52,941)
Balance, March 31, 2018	$	(22,473)
Financial performance		(3,159)
Item that will not be reclassified to financial performance		
Remeasurement of defined benefit plans (note 12)		14,878
Balance, June 30, 2018	$	(10,754)

The accompanying notes are an integral part of these condensed interim financial statements.

CANADIAN AIR TRANSPORT SECURITY AUTHORITY

Condensed Interim Statement of Cash Flows

(Unaudited)

(In thousands of Canadian dollars)

	Three months ended June 30	
	2019	2018
Cash flows provided by (used in)		
Operating activities		
Financial performance	$ (4,228)	$ (3,159)
Items not involving cash		
Depreciation of property and equipment (note 6 and 13)	15,663	15,008
Increase in net employee benefits liability	2,144	2,137
Loss on disposal of property and equipment	984	52
Depreciation of right-of-use assets (note 8 and 13)	910	-
Change in fair value of financial instruments at fair value through profit and loss	637	(114)
Amortization of intangible assets (note 7 and 13)	523	312
Write-off of property and equipment	79	250
Amortization of deferred government funding related to capital expenditures (note 11)	(17,208)	(15,587)
Other non-cash transactions	(1)	4
Deferred lease incentives recognized in financial performance	-	(24)
Net change in working capital balances (note 18)	40,194	65,275
	39,697	64,154
Investing activities		
Parliamentary appropriations received for capital funding (note 14)	63,872	27,200
Purchase of property and equipment	(25,466)	(38,719)
Purchase of intangible assets	(3,557)	(3,938)
	34,849	(15,457)
Financing activities		
Lease payments	(853)	-
	(853)	-
Increase in cash	73,693	48,697
Cash, beginning of period	4,007	9,929
Cash, end of period	$ 77,700	$ 58,626

Interest expense paid and interest income received approximate finance costs and finance income, respectively, in the Condensed Interim Statement of Comprehensive Income (Loss).

Supplementary cash flow information (note 18)

The accompanying notes are an integral part of these condensed interim financial statements.

1. Corporate information

CATSA is a Crown corporation listed under Part I, Schedule III of the *Financial Administration Act* and is an agent of Her Majesty in right of Canada. CATSA is responsible for securing specific elements of the air transportation system, from passenger and baggage screening to screening airport workers.

CATSA is funded by parliamentary appropriations and accountable to Parliament through the Minister of Transport. With the support of Transport Canada, CATSA entered into a Supplemental Screening Services agreement to trial cost recovery at PBS with the GTAA for the provision of supplemental screening services effective October 5, 2014, and extended annually thereafter. CATSA received approval from TC to extend the ongoing agreement with GTAA until March 31, 2020, pursuant to the authorities introduced by Bill C-49.

CATSA also entered into an agreement with the Muskoka Airport Authority to provide screening services over a 10-week period. Approval was obtained from TC and the 10-week period began in June 2019.

These condensed interim financial statements have been authorized for issuance by the Board of Directors on August 23, 2019.

2. Basis of preparation

The condensed interim financial statements have been prepared in accordance with Section 131.1 of the *Financial Administration Act* and International Accounting Standards 34 *Interim Financial Reporting* (IAS 34) as issued by the International Accounting Standards Board (IASB) and approved by the Accounting Standards Board of Canada.

Section 131.1 of the *Financial Administration Act* requires that most parent Crown corporations prepare and make public quarterly financial reports in compliance with the Treasury Board of Canada Secretariat's *Standard on Quarterly Financial Reports for Crown Corporations*. These condensed interim financial statements have not been audited or reviewed by CATSA's external auditor.

As permitted by IAS 34, these interim financial statements are presented on a condensed basis and therefore do not include all necessary disclosures to conform, in all material respects, with IFRS disclosure requirements applicable to annual financial statements. These condensed interim financial statements are intended to provide an update on the latest complete set of audited annual financial statements. Accordingly, they should be read in conjunction with the audited annual financial statements for the year ended March 31, 2019.

3. Summary of significant accounting policies

Significant accounting policies used in these condensed interim financial statements are disclosed in note 3 of CATSA's audited annual financial statements for the year ended March 31, 2019, with the exception of IFRS 16 *Leases*, which became effective for CATSA April 1, 2019.

IFRS 16 specifies how to recognize, measure, present and disclose leases. This standard introduces significant changes to the lessee accounting by removing the distinction between operating and finance leases and requiring the recognition of a right-of-use asset and lease liability at the lease commencement date for all leases, except for certain leases subject to exemption. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17 *Leases*.

CATSA has applied IFRS 16 using the modified retrospective approach and accordingly the prior period information has not been restated. CATSA also elected to record right-of-use assets based on the corresponding lease liability. Right-of-use assets and lease liabilities of $25,956 were recorded as of April 1, 2019, with no impact to equity. When measuring lease liabilities, CATSA discounted lease payments using its incremental borrowing rate as at April 1, 2019. The weighted-average incremental borrowing rate applied was 2.0%.

Based on the nature and use of CATSA's right-of-use assets, CATSA has two classes of underlying assets: office space and data centres.

CATSA has elected to apply the practical expedient available on transition to not reassess whether a contract is, or contains, a lease. Accordingly, the definition of a lease, in accordance with IAS 17 and IFRIC 4 *Determining whether an arrangement contains a lease,* will continue to be applied to leases entered into or modified prior to April 1, 2019. CATSA will apply the definition of a lease under IFRS 16 to all lease contracts entered into or modified on or after April 1, 2019.

CATSA has elected to apply the practical expedient available on transition to not recognize a right-of-use asset or lease liability for certain leases where the lease term ends within 12 months of transition. This assessment was made on a lease-by-lease basis. For leases where the practical expedient was applied, CATSA accounts for these leases in the same manner as short-term leases and the payments are recognized as an expense in the period in which they occurred.

See accounting policy note below for additional practical expedient choices.

(In thousands of Canadian dollars)

The following table reconciles CATSA's operating lease commitments as at March 31, 2019, as previously disclosed in CATSA's financial statements, to the lease liabilities recognized on initial application of IFRS 16 as at April 1, 2019:

Operating lease commitments as at March 31, 2019	$ 25,243
Discounted using incremental borrowing rate as at April 1, 2019	(2,246)
Variable lease payments that do not depend on an index or rate	(9,757)
Fixed operating costs related to data centre non-lease components[1]	(800)
Recognition exemption for short-term leases	(63)
Extension options reasonably certain to be exercised	13,579
Lease liabilities recognized as at April 1, 2019	$ 25,956

[1] Previously, under IFRIC 4 *Determining whether an Arrangement contains a Lease*, CATSA included fixed operating costs associated with one of its data centre leases in the measurement of its operating lease commitments. Under IFRS 16 these items are considered non-lease components and as such are excluded from the measurement of the lease liabilities.

As a result of the adoption of IFRS 16, the following updates have been made to CATSA's significant accounting policies:

<u>Use of estimates and judgments:</u>

The critical estimates and assumptions utilized in preparing these financial statements include:

- Right-of-use assets and lease liabilities

  Key estimates used for right-of-use assets and lease liabilities include the determination of an appropriate incremental borrowing rate to discount the lease payments, when the interest rate implicit in the lease is not readily determinable. As CATSA does not have borrowing authority and, in practice, does not have readily observable approved or granted borrowing rates from a financial institution, CATSA's approach to determining its incremental borrowing rate is based on the Bank of Canada zero-coupon bond rate, CATSA's entity-specific credit spread, and the lease-specific spread. CATSA's entity-specific credit spread and lease-specific spread are based on a publicly available yield curve that reflects Canadian agencies with investment grade ratings. The rate used to discount CATSA's lease payments is also based on the identified lease term.

The critical judgments made by management in preparing these financial statements include:

- Right-of-use assets and lease liabilities

  Judgments are required in determining whether it is reasonably certain that an extension or termination option will be exercised for contracts that are or contain a lease. In making this assessment, management considers a number of factors, including the nature of CATSA's work, proximity of other locations, lease extensions exercised in the past, market conditions, recent leasehold improvements and contract specific termination clauses.

  Judgments are required in determining whether variable lease payments are in-substance fixed. In-substance fixed lease payments are payments that may, in form, contain variability but that, in substance, are unavoidable. Such payments are included in the measurement of the lease liability. In determining whether variable lease payments are in-substance fixed, CATSA reviews lease contracts to assess the nature of the payments, specifically identifying if payments are subject to adjustments based on actual costs incurred, or payments are based on services that are variable in nature.

Accounting policy - Leases:

At the inception of a contract, CATSA assesses whether a contract is, or contains, a lease based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. If a lease is identified, CATSA recognizes a right-of-use asset and a lease liability at the lease commencement date.

The right-of-use asset is initially measured at cost based on the following:

- Amount of the initial measurement of the lease liability;
- Any lease payments made at or before the commencement date, less any lease incentives received;
- Any initial direct costs incurred; and
- An estimate of costs to dismantle and remove the underlying asset, or to restore the underlying asset or the site on which it is located.

The right-of-use asset is subsequently measured at cost less accumulated depreciation. The carrying amount of the right-of-use asset may be reduced by impairment losses, if any, and adjusted for certain remeasurement of the lease liability, if any.

The right-of-use asset is depreciated using the straight-line method over the shorter of the lease term or the estimated useful life of the underlying asset. The lease term includes periods covered by an option to extend if CATSA is reasonably certain to exercise that option.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, CATSA's incremental borrowing rate, as identified in the above use of estimates and judgments.

The lease payments included in the measurement of the lease liability are comprised of the following, where applicable:

- Fixed payments (including in-substance fixed payments, if any), less any lease incentives receivable;
- Variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- Amounts expected to be payable under residual value guarantees;
- Exercise price of a purchase option if it is reasonably certain that CATSA will exercise that; and
- Payments of penalties for terminating the lease, if the lease term reflects CATSA exercising an option to terminate the lease.

CATSA's entity-specific credit spread and lease-specific spread are based on a publicly available yield curve that reflects Canadian agencies with investment grade ratings.

Variable lease payments that do not depend on an index or rate, and are not in-substance fixed, are not included in the measurement of the lease liability and, subsequently, the right-of-use asset. These payments are recognized as an expense in the period in which they occur.

The lease liability is subsequently measured at amortized cost using the effective interest rate method. It is remeasured whenever:

- There is a change in the lease term, including a change in the assessment of whether an extension option will be exercised, in which case the lease liability is remeasured by discounting the revised lease payments on the basis of the revised lease term using a revised discount rate;
- The payments change due to changes in an index or rate, or a change in expected payments under a residual value guarantee, in which case the lease liability is remeasured by discounting the revised lease payments using the initial discount rate; and
- A lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.

(In thousands of Canadian dollars)

Based on the nature and use of CATSA's right-of-use assets, CATSA has two classes of underlying assets: office space and data centres. CATSA accounts for lease components and any non-lease components as a single lease component for its office space asset class. For its data centre asset class, CATSA separates non-lease components from lease components and accounts for them separately.

CATSA does not recognize right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less or are leases of low value. The lease payments associated with these leases are recognized as an expense on straight-line basis over the lease term.

4. Trade and other receivables

Trade and other receivables are comprised of:

	June 30, 2019	March 31, 2019
Parliamentary appropriations	$ 61,667	$ 131,926
GST and HST recoverable	9,115	9,142
PST recoverable	3,542	2,447
Screening services - supplemental	3,077	1,975
Screening services - other	25	-
	$ 77,426	$ 145,490

Credit terms on trade receivables are 30 days. As at June 30, 2019, and March 31, 2019, there were no amounts included in trade and other receivables that were past due.

5. Inventories

Inventories are comprised of:

	June 30, 2019	March 31, 2019
Spare parts	$ 13,293	$ 13,843
RAIC	1,031	313
Uniforms	528	1,149
	$ 14,852	$ 15,305

(In thousands of Canadian dollars)

6. Property and equipment

A reconciliation of property and equipment is as follows:

	PBS equipment	HBS equipment	NPS equipment	RAIC equipment	Computers, integrated software and electronic equipment	Office furniture and equip-ment	Leasehold improve-ments	Work-in-progress	Total
Cost									
Balance, March 31, 2018	$ 144,870	$ 689,803	$ 19,854	$ 4,439	$ 26,914	$ 30	$ 10,002	$ 79,092	$ 975,004
Additions	13,261	8,515	(16)	88	673	118	639	79,531	102,809
Disposals	(3,216)	(32,871)	(1,744)	-	(392)	-	(19)	-	(38,242)
Write-offs	(963)	(1,192)	-	(88)	(446)	(19)	(66)	(95)	(2,869)
Reclassifications	5,424	55,250	297	36	1,485	-	57	(62,572)	(23)
Balance, March 31, 2019	$ 159,376	$ 719,505	$ 18,391	$ 4,475	$ 28,234	$ 129	$ 10,613	$ 95,956	$ 1,036,679
Balance, March 31, 2019	$ 159,376	$ 719,505	$ 18,391	$ 4,475	$ 28,234	$ 129	$ 10,613	$ 95,956	$ 1,036,679
Additions	2,808	276	-	-	1	-	-	16,914	19,999
Disposals	(1,140)	(26,277)	-	-	(107)	-	-	-	(27,524)
Write-offs	(375)	-	-	(178)	(454)	-	-	-	(1,007)
Reclassifications	(4,534)	3,344	2,653	-	502	-	-	(1,965)	-
Balance, June 30, 2019	$ 156,135	$ 696,848	$ 21,044	$ 4,297	$ 28,176	$ 129	$ 10,613	$ 110,905	$ 1,028,147
Accumulated depreciation									
Balance, March 31, 2018	$ 87,764	$ 429,742	$ 11,016	$ 2,959	$ 18,108	$ 30	$ 8,947	$ -	$ 558,566
Depreciation	13,398	43,663	1,572	536	2,663	13	526	-	62,371
Disposals	(3,211)	(32,092)	(1,745)	-	(392)	-	(19)	-	(37,459)
Write-offs	(594)	(1,177)	55	(88)	(434)	(19)	(66)	-	(2,323)
Balance, March 31, 2019	$ 97,357	$ 440,136	$ 10,898	$ 3,407	$ 19,945	$ 24	$ 9,388	$ -	$ 581,155
Balance, March 31, 2019	$ 97,357	$ 440,136	$ 10,898	$ 3,407	$ 19,945	$ 24	$ 9,388	$ -	$ 581,155
Depreciation	3,388	10,907	426	138	700	6	98	-	15,663
Disposals	(1,088)	(25,346)	-	-	(106)	-	-	-	(26,540)
Write-offs	(295)	-	-	(178)	(454)	-	-	-	(927)
Reclassifications	(4,210)	2,542	1,668	-	-	-	-	-	-
Balance, June 30, 2019	$ 95,152	$ 428,239	$ 12,992	$ 3,367	$ 20,085	$ 30	$ 9,486	$ -	$ 569,351
Carrying amounts									
As at March 31, 2019	$ 62,019	$ 279,369	$ 7,493	$ 1,068	$ 8,289	$ 105	$ 1,225	$ 95,956	$ 455,524
As at June 30, 2019	$ 60,983	$ 268,609	$ 8,052	$ 930	$ 8,091	$ 99	$ 1,127	$ 110,905	$ 458,796

(In thousands of Canadian dollars)

7. Intangible assets

A reconciliation of intangible assets is as follows:

	Externally acquired software	Internally developed software	Under development	Total
Cost				
Balance, March 31, 2018	$ 4,494	$ 19,655	$ 3,241	$ 27,390
Additions	4,633	288	3,886	8,807
Write-offs	(30)	(2,285)	-	(2,315)
Reclassifications	23	2,550	(2,550)	23
Balance, March 31, 2019	$ 9,120	$ 20,208	$ 4,577	$ 33,905
Balance, March 31, 2019	$ 9,120	$ 20,208	$ 4,577	$ 33,905
Additions	-	21	895	916
Reclassifications	-	154	(154)	-
Balance, June 30, 2019	$ 9,120	$ 20,383	$ 5,318	$ 34,821
Accumulated amortization				
Balance, March 31, 2018	$ 3,338	$ 15,387	$ -	$ 18,725
Amortization	697	1,083	-	1,780
Write-offs	(30)	(2,285)	-	(2,315)
Balance, March 31, 2019	$ 4,005	$ 14,185	$ -	$ 18,190
Balance, March 31, 2019	$ 4,005	$ 14,185	$ -	$ 18,190
Amortization	190	333	-	523
Balance, June 30, 2019	$ 4,195	$ 14,518	$ -	$ 18,713
Carrying amounts				
As at March 31, 2019	$ 5,115	$ 6,023	$ 4,577	$ 15,715
As at June 30, 2019	$ 4,925	$ 5,865	$ 5,318	$ 16,108

(In thousands of Canadian dollars)

8. Right-of-use assets

A reconciliation of right-of-use assets is as follows:

	Office space	Data centres	Total
Balance, April 1, 2019	$ 24,223	$ 1,733	$ 25,956
Deferred lease incentives adjustment	(482)	-	(482)
Additions	7	-	7
Depreciation	(858)	(52)	(910)
Balance, June 30, 2019	$ 22,890	$ 1,681	$ 24,571

9. Provisions and contingencies

(a) Provisions

Several claims, audits and legal proceedings have been asserted or instituted against CATSA. By nature, these amounts are subject to many uncertainties and the outcome of individual matters is not always predictable. Provisions are determined by taking into account internal analysis, consultations with external subject matter experts, and all available information at the time of financial statement preparation.

There were no provisions recorded as at June 30, 2019, or March 31, 2019.

(b) Contingencies

CATSA's contingent liabilities consist of claims and legal proceedings and decommissioning costs for which no provision is recorded.

(i) Claims and legal proceedings

In 2017/18, CATSA received notification from an airport authority that it had been assessed by the Canada Revenue Agency for failing to charge HST to CATSA on funding agreements related to integration projects and maintenance agreements. With the cooperation of the airport authority, CATSA filed a notice of objection and is of the view that it is more likely than not that the notice of objection will be successful. Should the objection prove to be successful, CATSA will be able to recover all amounts remitted related to this assessment.

CATSA has similar funding agreements with other airport authorities that could result in an assessment by tax authorities. While CATSA judges that the likelihood of economic outflow related to these other funding agreements to be not probable, there is a risk that CATSA could be required to pay other assessments in the event that these other airport authorities are audited and the Canada Revenue Agency upholds its position. The maximum undiscounted cash flow that could be required to settle this contingent liability is estimated to be $22,388 (March 31, 2019 – $20,950), offset by estimated recoverable taxes of $10,512 (March 31, 2019 – $9,980) for a net amount of $11,876 (March 31, 2019 – $10,970). These amounts have not been recorded in the financial statements.

(ii) Decommissioning costs

During the three months ended June 30, 2019, there have been no material changes to contingencies related to decommissioning costs. For a description of CATSA's decommissioning costs, refer to note 8(b)(ii) of the audited annual financial statements for the year ended March 31, 2019.

(In thousands of Canadian dollars)

10. Lease liabilities

CATSA has leases that are for office space and data centres. CATSA has included extension options in the measurement of its lease liabilities when it is reasonably certain to exercise the extension option.

A reconciliation of lease liabilities is as follows:

Balance, April 1, 2019	$	25,956
Additions		7
Lease payments		(981)
Finance costs		128
Foreign exchange revaluation		(2)
Balance, June 30, 2019	$	25,108
Balance, June 30, 2019		
Current	$	3,433
Non-current		21,675

For the three months ended June 30, 2019, CATSA recognized an expense of $600 relating to variable lease payments not included in the measurement of lease liabilities. This amount includes variable lease payments for operating costs, property taxes, insurance, and other service-related costs. For the three months ended June 30, 2019, CATSA recognized an expense of $17 relating to short-term leases, and $22 relating to leases of low value assets. For the three months ended June 30, 2019, CATSA recognized a total cash outflow for leases of $1,620.

The following table presents the undiscounted cash flows for contractual lease obligations as at June 30, 2019:

No later than 1 year	$	6,892
Later than 1 year and no later than 5 years		15,484
Later than 5 years		461
Total	$	22,837

(In thousands of Canadian dollars)

11. Deferred government funding

A reconciliation of the deferred government funding liability is as follows:

	June 30, 2019	March 31, 2019
Deferred government funding related to operating expenses		
Balance, beginning of period	$ 18,558	$ 19,534
Operating expenses funded through parliamentary appropriations	175,367	703,073
Parliamentary appropriations recognized as government funding for operating expenses	(175,864)	(704,049)
Balance, end of period	$ 18,061	$ 18,558
Deferred government funding related to capital expenditures		
Balance, beginning of period	$ 469,732	$ 424,026
Capital expenditures funded through parliamentary appropriations	20,869	110,853
Government funding received in advance	5,450	-
Amortization of deferred government funding related to capital expenditures	(17,208)	(65,147)
Balance, end of period	$ 478,843	$ 469,732
Total deferred government funding, end of period	$ 496,904	$ 488,290

For additional information on government funding, see note 14.

(In thousands of Canadian dollars)

12. Employee benefits

(a) Employee benefits asset and liability

Employee benefits asset and liability recognized and presented in the Condensed Interim Statement of Financial Position are detailed as follows:

	June 30, 2019	March 31, 2019
Employee benefits asset		
Registered pension plan (RPP)	$ -	$ 3,931
Supplementary retirement plan (SRP)	1,246	1,797
	1,246	5,728
Employee benefits liability		
Registered pension plan (RPP)	(17,918)	-
Other defined benefits plan (ODBP)	(35,325)	(30,507)
	(53,243)	(30,507)
Employee benefits - net liability	$ (51,997)	$ (24,779)

(In thousands of Canadian dollars)

(b) Employee benefits costs

The elements of employee benefits costs are as follows:

	For the three months ended June 30							
	RPP		SRP		ODBP		Total	
	2019	2018	2019	2018	2019	2018	2019	2018
Defined benefit cost recognized in financial performance								
Current service cost	$ 2,137	$ 2,244	$ 24	$ 17	$ 467	$ 462	$ 2,628	$ 2,723
Administration costs	75	62	4	4	-	-	79	66
Interest cost on defined benefit obligation	1,854	1,775	45	44	282	264	2,181	2,083
Interest income on plan assets	(1,816)	(1,728)	(60)	(58)	-	-	(1,876)	(1,786)
Defined benefit cost	$ 2,250	$ 2,353	$ 13	$ 7	$ 749	$ 726	$ 3,012	$ 3,086
Remeasurement of defined benefit plans recognized in other comprehensive income (loss)								
Return on plan assets excluding interest income	$ 4,709	$ 1,982	$ 13	$ 100	$ -	$ -	$ 4,722	$ 2,082
Actuarial (losses) gains	(25,138)	10,865	(551)	207	(4,107)	1,724	(29,796)	12,796
Remeasurement of defined benefit plans	$ (20,429)	$ 12,847	$ (538)	$ 307	$ (4,107)	$ 1,724	$ (25,074)	$ 14,878

For the three months ended June 30, 2019, CATSA recognized an expense of $177 (2018 - $142) in relation to the defined contribution component of the RPP.

(c) Significant actuarial assumptions

Assumptions used to measure the defined benefit plan assets and liabilities are reviewed and, as necessary, revised at each reporting period. This typically includes reviewing the discount rates and actual rate of return on the plan assets against rates previously estimated, to reflect the current assumptions and circumstances. Changes to actuarial assumptions result in remeasurement gains and/or losses recognized in other comprehensive income (loss).

For the three months ended June 30, 2019, remeasurement losses of $25,074 resulted from a decrease in the discount rate of 50 basis points (from 3.50% at March 31, 2019 to 3.00% at June 30, 2019). This was partially offset by higher actual rates of return on plan assets than the rates used in CATSA's assumptions (3.27% actual versus 0.88% expected for the RPP and 0.97% actual versus 0.88% expected for the SRP).

(In thousands of Canadian dollars)

For the three months ended June 30, 2018, remeasurement gains of $14,878 resulted primarily from an increase in the discount rate of 25 basis points (from 3.50% at March 31, 2018 to 3.75% at June 30, 2018). The gain was also due to higher actual rates of return on plan assets than the rates used in CATSA's assumptions (1.90% actual versus 0.88% expected for the RPP and 2.39% actual versus 0.88% expected for the SRP).

(d) Employer contributions

Employer contributions paid to the defined benefit plans for the three months ended June 30 are presented as follows:

	Three months ended June 30	
	2019	2018
Employer contributions		
RPP	$ 830	$ 917
ODBP	38	32
	$ 868	$ 949

Total employer contributions to the defined benefit plans are estimated to be $4,110 for the year ending March 31, 2020.

(In thousands of Canadian dollars)

13. Expenses

The Condensed Interim Statement of Comprehensive Income (Loss) presents operating expenses by program activity. The following table presents operating expenses by major expense type for the three months ended June 30:

	Three months ended June 30	
	2019	2018
Screening services and other related costs		
Payments to screening contractors	$ 149,282	$ 143,288
Uniforms and other screening costs	1,434	1,399
Trace and consumables	599	445
	151,315	145,132
Equipment operating and maintenance		
Equipment maintenance and spare parts	10,032	9,354
Training and certification	246	241
RAIC	210	271
	10,488	9,866
Program support and corporate services		
Employee costs	16,795	16,284
Office and computer expenses	2,218	1,100
Professional services and other business related costs	1,650	1,355
Other lease costs (note 10)	639	-
Operating leases	-	1,566
Other administrative costs	617	1,045
Communications and public awareness	164	109
	22,083	21,459
Depreciation and amortization		
Depreciation of property and equipment (note 6)	15,663	15,008
Depreciation of right-of-use assets (note 8)	910	-
Amortization of intangible assets (note 7)	523	312
	17,096	15,320
	$ 200,982	$ 191,777

Other business related costs include travel expenses, conference fees, membership and association fees, and meeting expenses. Other administrative costs include insurance, network and telephone expenses, and facilities maintenance.

(In thousands of Canadian dollars)

14. Government funding

CATSA's corporate plan for the current fiscal year has not yet been tabled in Parliament and, therefore, the total amount of parliamentary appropriations available for the current year is not yet publicly available. As a result, disclosure of parliamentary appropriations approved compared to parliamentary appropriations used has not been provided.

The following table reconciles parliamentary appropriations for operating expenses that were received and receivable with the amount of appropriations used during the three months ended June 30:

	Three months ended June 30	
	2019	2018
Parliamentary appropriations received and receivable	$ 269,740	$ 275,363
Amounts received and receivable related to prior periods	(94,373)	(107,407)
Amounts to be used in future periods	-	(1,477)
Parliamentary appropriations used to fund operating expenses (note 11)	$ 175,367	$ 166,479

The following table reconciles parliamentary appropriations related to capital expenditures that were received and receivable with the amount of appropriations used during the three months ended June 30:

	Three months ended June 30	
	2019	2018
Parliamentary appropriations received and receivable	$ 63,872	$ 50,483
Parliamentary appropriations received and receivable - lease payments	981	-
Amounts received and receivable related to prior periods	(37,553)	(13,992)
Amounts to be (used) billed in future periods	(5,450)	1,864
Parliamentary appropriations used to fund capital expenditures	$ 21,850	$ 38,355

Parliamentary appropriations to be billed (used) in future periods are a result of lower (higher) forecasted expenditures than actual operating and capital expenditures. These amounts are expected to be billed (used) within the next fiscal quarter.

(In thousands of Canadian dollars)

15. Fair values of financial instruments

Derivative financial instruments are recorded at fair value on the Condensed Interim Statement of Financial Position. The fair values of cash, receivables related to screening services, trade and other payables, and current holdbacks approximate their carrying amount due to the current nature of these instruments.

The carrying amounts and corresponding fair values of CATSA's remaining financial assets and liabilities are as follows:

	June 30, 2019		March 31, 2019	
	Carrying Amount	Fair Value (Level 2)	Carrying Amount	Fair Value (Level 2)
Financial instruments measured at fair value				
Derivative financial assets[1]	$ -	$ -	$ 537	$ 537
Derivative financial liabilities[1]	100	100	-	-
Financial instruments measured at amortized cost				
Non-current holdbacks[2]	$ 8,490	$ 8,490	$ 7,767	$ 7,767

[1] The fair value is based on a discounted cash flow model based on observable inputs.
[2] The fair value is determined using expected future cash flows, discounted using published Government of Canada bond rates with similar terms and characteristics.

There were no transfers between levels during the three months ended June 30, 2019, or year ended March 31, 2019.

(In thousands of Canadian dollars)

16. Contractual arrangements

In the normal course of operations, CATSA enters into contractual arrangements for the supply of goods and services. These contractual arrangements are subject to authorized appropriations and termination rights which allow CATSA to terminate the contracts without penalty at its discretion. The most significant arrangements relate to contracts signed with screening contractors for the provision of screening services, as well as with vendors for screening equipment and related maintenance.

The following table provides the remaining pre-tax balance on these contractual arrangements:

	June 30, 2019	March 31, 2019
Operating	$ 1,495,682	$ 1,626,045
Capital	79,299	111,938
Total	$ 1,574,981	$ 1,737,983

(In thousands of Canadian dollars)

17. Related party transactions

CATSA had the following transactions with related parties for the three months ended June 30, 2019:

(a) Government of Canada, its agencies and other Crown corporations

CATSA is wholly owned by the Government of Canada and is under common control with other Government of Canada departments, agencies and Crown corporations. CATSA enters into transactions with these entities in the normal course of operations. These related party transactions are based on normal trade terms applicable to all individuals and corporations.

The following table summarizes CATSA's transactions with related parties:

	Three months ended June 30	
	2019	2018
Operating		
Income	$ 194,053	$ 184,080
Expenses	3,883	4,874
Capital		
HBS equipment	439	-

Income from related parties represent parliamentary appropriations for operating expenses, parliamentary appropriations for lease payments, and amortization of deferred government funding related to capital expenditures. Expenses presented above for the three months ended June 30, 2019, include $4,044 (2018 – $4,569) in non-recoverable taxes paid to fiduciaries of the Canada Revenue Agency.

The following related party balances are included in trade and other receivables and trade and other payables, respectively, on the Condensed Interim Statement of Financial Position:

	June 30, 2019	March 31, 2019
Receivable from related parties	$ 70,782	$ 141,068
Payable to related parties	(1,346)	(1,394)
Net receivable from related parties	$ 69,436	$ 139,674

(In thousands of Canadian dollars)

Amounts receivable from related parties consist primarily of $61,667 (March 31, 2019 – $131,926) due from the Government of Canada for parliamentary appropriations used during the period and not received at the end of period, and $9,115 (March 31, 2019 – $9,142) due from the Canada Revenue Agency for recoverable taxes paid on expenses. Amounts payable to related parties consist primarily of indirect taxes payable to the Canada Revenue Agency.

(b) Transactions with CATSA's post-employment benefit plans

Transactions with the RPP, SRP and ODBP are conducted in the normal course of business. The transactions with CATSA's post-employment benefit plans consist of contributions as disclosed in note 12. No other transactions were made during the three month period.

18. Net change in working capital balances and supplementary cash flow information

The following table presents the net change in working capital balances for the three months ended June 30:

	Three months ended June 30	
	2019	2018
Decrease in trade and other receivables	$ 30,511	$ 40,337
Decrease in inventories	453	1,809
Decrease in prepaids	44	205
Increase in trade and other payables	9,683	24,938
Decrease in deferred government funding related to operating expenses	(497)	(2,014)
	$ 40,194	$ 65,275

The change in trade and other receivables excludes an amount of $37,553 (2018 – $11,155) in relation to government funding related to capital expenditures, as the amount relates to investing activities.

The change in prepaids excludes an amount of $676 (2018 – $Nil) in relation to the acquisition of property and equipment, as the amount relates to investing activities.

The change in trade and other payables excludes an amount of $9,878 (2018 – $5,299) in relation to the acquisition of property and equipment and intangible assets, as the amount relates to investing activities.

19. Budget 2019 and the Security Screening Services Commercialization Act

As part of Budget 2019, the Government of Canada announced its intention to introduce legislation to enable the creation of an independent, not-for-profit entity, established by industry, which will assume the responsibility for aviation screening at Canada's airports. The *Security Screening Services Commercialization Act* (SSSCA) was tabled as part of Bill C-97 and received Royal Assent in June 2019. The SSSCA allows for the sale of CATSA's assets and liabilities and the transfer of screening operations to the new entity.

These developments have not changed CATSA's mandate. CATSA will continue to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.