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**KARMA CO-OPERATIVE INC.**

**FINANCIAL STATEMENTS**

**MAY 31, 2018**



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**FINANCIAL STATEMENTS**

**MAY 31, 2018**

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## INDEPENDENT AUDITORS' REPORT

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To the Members of  
**Karma Co-Operative Inc.**

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Karma Co-Operative Inc., which comprise the statement of financial position as at May 31, 2018, and the statements of net assets, operations, and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian accounting standards for not-for-profit organizations, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditor's Responsibility*

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

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

**INDEPENDENT AUDITORS' REPORT (Continued)**

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

*Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of Karma Co-Operative Inc. as at May 31, 2018 and the results of its operations and its cash flows for the year then ended, in accordance with Canadian accounting standards for not-for-profit organizations.

**KRIENS~LAROSE, LLP**



**Chartered Professional Accountants  
Licensed Public Accountants**

Toronto, Ontario  
September 23, 2018

KARMA CO-OPERATIVE INC.  
**STATEMENT OF FINANCIAL POSITION**  
AS AT MAY 31, 2018

Page 3

	2018	2017
	\$	\$
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash	4,764	6,799
Accounts receivable	3,313	-
Inventory	116,655	113,621
Prepaid expenses (Note 3)	28,652	1,185
Membership loan - ONFC (Note 4)	-	35,000
	153,384	156,605
<b>PROPERTY AND EQUIPMENT (Note 5)</b>	181,146	199,748
<b>INVESTMENTS (Note 2)</b>	2,225	2,223
	336,755	358,576

(Continued on the next page)

See accompanying notes to the financial statements

KARMA CO-OPERATIVE INC.  
**STATEMENT OF FINANCIAL POSITION**  
AS AT MAY 31, 2018

	2018	2017
	\$	\$
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable	81,516	78,364
Current portion of building loans (Note 9)	5,000	12,500
Deferred revenue (Note 6)	6,236	5,941
Bank term loan (Note 7)	5,482	5,247
Bank line of credit (Note 7)	-	1,072
	98,234	103,124
<b>LONG TERM</b>		
Bank term loan (Note 6)	79,364	84,843
Building loans (Note 9)	22,500	20,000
	200,098	207,967
<b>NET ASSETS</b>		
<b>UNRESTRICTED NET ASSETS</b>	56,881	63,437
<b>MEMBERSHIP LOANS (NOTE 8)</b>	79,776	87,172
	136,657	150,609
	336,755	358,576

APPROVED ON BEHALF OF THE BOARD:

\_\_\_\_\_, Director

\_\_\_\_\_, Director

KARMA CO-OPERATIVE INC.  
**STATEMENT OF NET ASSETS**  
AS AT MAY 31, 2018

	Unrestricted Net assets \$	Member Loans (Note 8) \$	Total 2018 \$	Total 2017 \$
Balance, beginning of year	63,437	87,172	150,609	171,123
(Deficiency) of retail revenues over expenses for the year	(21,308)	-	(21,308)	(20,729)
Excess (deficiency) of membership revenues over expenses for the year	5,086	-	5,086	(134)
Member loans received - net	-	2,270	2,270	349
Forfeited member loans (Note 8)	9,666	(9,666)	-	-
Balance, end of year	56,881	79,776	136,657	150,609

See accompanying notes to the financial statements

KARMA CO-OPERATIVE INC.  
**CONSOLIDATED STATEMENT OF OPERATIONS**  
FOR THE YEAR ENDED MAY 31, 2018

Page 6

	2018	2017
	\$	\$
<b>REVENUES</b>		
GROSS PROFIT FROM RETAIL OPERATIONS	322,854	326,725
MISCELLANEOUS OPERATIONS REVENUE	24,814	11,275
MEMBER SERVICE FEES REVENUE	12,900	9,564
	360,568	347,564
<b>EXPENSES</b>		
OPERATIONS EXPENSES	368,976	358,729
MEMBERSHIP EXPENSES	7,814	9,698
	376,790	368,427
<b>(DEFICIENCY) OF REVENUE OVER EXPENSES FOR THE YEAR</b>	<b>(16,222)</b>	<b>(20,863)</b>

See accompanying notes to the financial statements



KARMA CO-OPERATIVE INC.  
**STATEMENT OF RETAIL OPERATIONS**  
 FOR THE YEAR ENDED MAY 31, 2018

	2018	2017
	\$	\$
<b>SALES</b> (Note 6, 11)	1,325,301	1,357,167
<b>COST OF SALES</b>		
Inventory - beginning of year	113,621	109,864
Purchases	1,005,481	1,034,199
Inventory - end of year	(116,655)	(113,621)
	1,002,447	1,030,442
<b>GROSS PROFIT</b>	322,854	326,725
<b>EXPENSES</b>		
Store wages and payroll costs	256,715	242,549
Amortization	22,664	25,889
Utilities	20,932	24,924
Office and general	17,040	22,041
Realty taxes	15,577	13,037
Repairs and maintenance	11,069	13,178
Marketing	10,093	1,548
Audit fees	7,200	7,200
Interest on long-term debt	4,366	4,917
Insurance	3,320	3,446
<b>TOTAL EXPENSES</b>	368,976	358,729
<b>(DEFICIENCY) OF RETAIL REVENUES OVER EXPENSES FOR THE YEAR</b>	(46,122)	(32,004)
<b>ADD</b>		
Current year's building fees and donations	12,900	9,564
Sundry revenue (Note 12)	11,914	1,711
<b>(DEFICIENCY) OF RETAIL REVENUES OVER EXPENSES FOR THE YEAR</b>	(21,308)	(20,729)

See accompanying notes to the financial statements

KARMA CO-OPERATIVE INC.  
**STATEMENT OF MEMBERSHIP OPERATIONS**  
FOR THE YEAR ENDED MAY 31, 2018

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	2018	2017
	\$	\$
<b>REVENUE</b>		
Member service fees (Note 6)	12,900	9,564
<b>EXPENSES</b>		
Administration	2,460	2,643
Committee	2,170	2,193
Audit fees	1,950	1,800
Other	1,234	1,320
Newsletter	-	1,742
	7,814	9,698
<b>EXCESS (DEFICIENCY) OF MEMBERSHIP REVENUE OVER EXPENSES FOR THE YEAR</b>	5,086	(134)

See accompanying notes to the financial statements

KARMA CO-OPERATIVE INC.  
**STATEMENT OF CASH FLOWS**  
 FOR THE YEAR ENDED MAY 31, 2018

	2018	2017
	\$	\$
<b>CASH WAS PROVIDED BY (USED IN):</b>		
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash receipts from retail operations sales	1,325,301	1,357,167
Cash receipts from membership and building fees	13,195	18,478
Cash receipts from other	24,814	1,711
Cash paid to suppliers and employees	(1,387,235)	(1,363,807)
	(23,925)	13,549
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of equipment	(4,064)	(3,496)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Increase (decrease) in bank line of credit	(1,072)	1,032
Member loans received - net of repayment	37,270	-
Increase (decrease) in bank term loan	(5,244)	(5,023)
Repayment of building loans	(5,000)	(6,000)
	25,954	(9,991)
<b>Change in cash</b>	(2,035)	62
<b>Cash, beginning of year</b>	6,799	6,737
<b>Cash, end of year</b>	4,764	6,799

See accompanying notes to the financial statements

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## PURPOSE OF THE CO-OPERATIVE

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Karma Co-operative Inc. is a not-for-profit organization incorporated under the Co-operative Corporations Act of Ontario.

Founded in 1972, Karma is a member-owned, democratically run co-operative. Karma specializes in organic, local, non-GMO and fair trade products.

The Co-operative is a not-for-profit entity under the Income Tax Act (Canada) and as such, is exempt from the payment of income taxes under section 149(1)(l) of the Income Tax Act (Canada).

### 1. SIGNIFICANT ACCOUNTING POLICIES

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The financial statements were prepared in accordance with Canadian accounting standards for not-for-profit organizations in Part III of the CPA Handbook and include the following significant accounting policies:

#### **Financial Instruments**

The Co-operative initially measures its financial assets and liabilities at fair value. The Co-operative subsequently measures all its financial assets and financial liabilities at amortized cost. Changes in fair value are recognized in the statement of operations.

Financial assets measured at cost include inventory.

Financial liabilities measured at cost include bank line of credit, bank term loan, accounts payable and accrued liabilities, and building loans.

#### **Use of Estimates**

The preparation of financial statements in accordance with Canadian accounting standards for not-for-profit organizations requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the reporting date and the reported amounts of revenues and expenses for the reporting period. Actual results could differ from these estimates. Significant financial statement items that require the use of estimates are useful lives of property and equipment, rates of amortization, accrued receivables and accrued liabilities. These estimates are reviewed periodically and adjustments are made, as appropriate, in the statement of operations in the year they become known.

#### **Cash and Cash Equivalents**

Cash and cash equivalents are defined as cash and short-term investments with maturity dates of less than 90 days.

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1. **SIGNIFICANT ACCOUNTING POLICIES (Continued)**

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**Inventory**

Inventory is generally valued at the last cost price paid for the same stock item, whether or not any of that item was purchased at a different wholesale cost. As it is impractical to isolate all discounted items which cannot be sold at the full intended price, during the inventory count the non-perishable discounted items are simply excluded from the inventory count, a process which approximately adjusts the total value of all discounted items to their net realizable value.

**Prepaid Expenses**

Prepaid expenses are recorded for goods and services being received in the next fiscal year but paid for in the current fiscal year.

**Property and Equipment and Amortization**

Property and equipment is recorded at acquisition cost.

Amortization is calculated on a straight-line basis over the total usage year of the equipment as following:

Building	40 years
Building improvements	20 years
Furniture & equipment	5 years
Computer equipment	3 years

Where equipment no longer has any long-term service potential to the Co-operative, the excess of its net carrying amount over any residual value is recognized as an expense in the statement of operations.

**Revenue Recognition**

The Co-operative follows the deferral method of accounting for contributions. Unrestricted contributions are recognized as revenue when received or receivable if the amount to be received can be reasonably estimated, and collection is reasonably assured.

Retail sales are recognized as revenue when received.

Membership fees are recognized monthly as each month of the membership fees' prepaid term elapses, with the remainder of the fees collected treated as deferred revenue.

All other revenues, with the exception of interest, are recognized as revenue when the transaction takes place.

Interest income is recognized as revenue when received.

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1. **SIGNIFICANT ACCOUNTING POLICIES (Continued)**

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**Unpaid receipts of materials and services**

The Co-operative does not account for the occasional, financially immaterial donations of materials which it receives. It also does not account on this statement for the substantial contributions of member labour it receives, of which most but not all is to fulfill work obligations as a condition of membership.

2. **INVESTMENTS**

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Investments consist of the following:

	2018	2017
	\$	\$
One membership share and 15 preference shares in Toronto Renewable Energy Co-operative	2,000	2,000
Shares in Alerna Savings and Credit Union Limited	225	223
	2,225	2,223

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3. **PREPAID EXPENSES**

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The increase in the prepaid expense balance is largely attributed to the purchase of bulk bins and display shelving that were received subsequent to year-end in June 2018.

4. **MEMBERSHIP LOAN-ONFC**

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The ONFC has been purchased by the Horizon Group, which is not a membership organization, and which committed in March 2017 to return each member's loan. The loan value was received on August 2, 2017.

Continued...

**5. PROPERTY AND EQUIPMENT**

	2018		2017	
	Cost \$	Accumulated amortization \$	Cost \$	Accumulated amortization \$
Building improvements	291,112	135,934	393,118	223,384
Computer equipment	7,290	6,779	7,290	6,256
Furniture	9,866	9,866	9,866	9,866
Building	40,000	40,000	40,000	40,000
Equipment	162,746	143,701	158,684	136,116
Land	6,412	-	6,412	-
	517,426	336,280	615,370	415,622
Net book value	181,146		199,748	

Some fully depreciated assets no longer in use by the Co-operative were removed from the 2018 figures, with no resulting change to the net book value.

**6. MEMBERSHIP FEES ALLOCATION AND REVENUE RECOGNITION**

The deferred revenue balance consists of the current fiscal year's portion of membership fees received. Income is recognized monthly as each month of the membership fees' prepaid term elapses, with the remainder of the fees collected treated as deferred revenue.

All membership fees received are divided evenly into building fees, appearing on the statement of retail operations, and member services fees, appearing on the statement of membership operations.

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7. **BANK LOANS**

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Karma has secured credit from Alterna Savings and Credit Union Limited, originally in the form of only a line of credit, but restructured during the 2016 fiscal year into a line of credit and a separate term loan. The purpose of the credit was to finance certain renovations to the Co-operative's property as approved by the Board of Directors.

**LINE OF CREDIT**

The line of credit is limited to a maximum of \$100,000 (current balance - \$0) and secured by an open first mortgage on the Co-operative's property located at 739 Palmerston Avenue, Toronto, Ontario. Interest is payable monthly at a variable rate calculated at Alterna Savings' prime rate plus 1.5%.

**BANK TERM LOAN**

	2018	2017
	\$	\$
Balance outstanding	84,846	90,090
Deduct- current portion	5,482	5,247
<hr/>		
Long-term portion	79,364	84,843

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The outstanding principal bears interest at a rate of 4.5%, and the outstanding principal will be \$73,637 when the loan is renewed on June 30, 2020. The loan is secured by a first mortgage on the Co-operative's property located at 739 Palmerston Avenue, Toronto, Ontario. The annual loan payments are \$9,154.

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**8. MEMBERSHIP LOANS**

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The Co-operative has recorded all membership loans received from its inception (1972) to date in its accounts. The loans payable to active members amount to \$79,776 (2017 - \$87,172). While reasonable effort has been made to repay membership loans to terminated members, the Co-operative has, for accounting purposes, adopted the policy of treating as forfeit all outstanding loans from members who have been inactive for eight years or more. The Board of Directors determined that of the total of membership loans, \$9,666 (2017: \$7,304) will not be repaid and were treated as forfeited to the Co-operative and therefore included as unrestricted net assets.

**9. BUILDING LOANS**

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The building loans have been issued in two series, with identical terms except for the maximum values of the individual loans. In 2008 and 2009, loans with no specified individual lending limit were received according to the terms of the Offering Statement of Karma Co-operative, Inc. dated May 31, 2008. Beginning in 2011, loans not exceeding \$1,000 per member per year were received according to the terms of Regulation 178 of the Revised Regulations of Ontario, Section 12.6, which allows loans of that value to be received from members without issuing an offering statement.

Interest is calculated using a rate per annum which is 50 basis points higher than the rate which Alterna Savings and Credit Union is paying for its investment savings account, as of the last day of the month. Interest is paid on the last day of the fiscal year. For the loans received before 2011, this represents a 25 basis point increase over the terms of the original offering statement, with the increase effective in August, 2011.

Although called building loans, reflecting their original use in financing renovations, the loans are not secured by a mortgage on the building or by any other security; they rank equally with all other unsecured debt.

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**10. TRANSACTIONS WITH NON-MEMBERS**

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Management estimates the amount of business transacted during the year with non-members was 10%.

**11. FLAT FEES AND SURCHARGES**

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Working and work-exempt members of the Co-operative pay a base price for their purchases. Non-members and members who elect not to work pay either a flat monthly fee or a percentage surcharge over that base price; these are both considered lieu-of-work fees. The sales figures reported on the statement of retail operations include the lieu-of-work fees, which are shown separately here.

	2018	2017
	\$	\$
Sales of goods before lieu-of-work fees	1,291,629	1,325,200
Lieu of work fees	33,672	31,967
<hr/>		
Total sales	1,325,301	1,357,167
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**12. SUNDRY REVENUE**

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The increase in sundry revenue is from a donation from two members to cover the cost associated with a marketing strategy and signage.

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**13. STATEMENT OF LIQUIDITY**

	2018	2017	Change
	\$	\$	\$
<b>Sources of liquidity</b>			
Alterna Savings line of credit			
Credit limit	100,000	100,000	-
Credit used	-	(1,072)	(1,072)
Remaining credit available	100,000	98,928	1,072
Cash	4,764	6,799	(2,035)
Current receivables	3,313	-	3,313
<b>Total sources</b>	<b>108,077</b>	<b>105,727</b>	<b>2,350</b>
<b>Demands upon liquidity</b>			
Accounts payable	81,516	78,364	3,152
Current portion of building loans	5,000	12,500	(7,500)
Current portion of bank term loan	5,482	5,247	235
<b>Total demands</b>	<b>91,998</b>	<b>96,111</b>	<b>(4,113)</b>
<b>Net liquidity</b>	<b>16,079</b>	<b>9,616</b>	<b>6,463</b>

The Statement of Liquidity provides another perspective on the flow of cash, other liquid assets, and short-term liabilities, showing our year-end ability to meet our year-end debts that will come due within the next year. Because the Co-operative has an operating line of credit, the actual cash on hand does not vary much. Instead, cash tends to flow out during periods of lower income and higher expenses, while cash flows in during periods of higher income and lower expenses. In both cases, the flow of cash primarily adjusts our credit usage rather than staying as cash. This can be summarized by net liquidity, the degree to which our cash and unused credit combined exceeds the Co-operative's short-term cash commitments.

Assets and liabilities for which cash has already been received or spent do not affect the Statement of Liquidity except through their effect on cash or available credit. In particular, the cash already received for future membership months, shown as a liability, is not treated like accounts payable, while cash already spent for prepaid expenses (such as insurance), shown as an asset, is not treated like accounts receivable. Also, the Co-operative does not consider its unused credit card limit as a source of liquidity and treats the credit card as a payment mechanism, not as a source of working capital.

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#### 14. FINANCIAL INSTRUMENTS

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The Co-operative is exposed to various risks through its financial instruments. The following presents the Co-operative's risk exposures and concentrations at May 31, 2018.

##### **Credit Risk**

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Co-operative's credit risk would occur with their accounts receivable. Actual exposure to credit losses has been minimal in prior years. The allowance for doubtful accounts is \$0 (2017: \$0).

##### **Liquidity Risk**

Liquidity risk is the risk the Co-operative will encounter difficulties in meeting obligations associated with financial liabilities. The Co-operative's exposure to liquidity risk is mainly in respect of its accounts payable. The Co-operative expects to meet these obligations as they come due by generating sufficient cash flow from operations. There has been no change in the risk assessment from the prior period (Note 13).

##### **Market Risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risks: currency risk, interest rate risk and other price risk. The Co-operative does not invest in financial instruments and is not subject to any of these risks.