

# Watson Folkins Corey LLP

Chartered Accountants  
70 Gloucester Street, Suite 106  
Ottawa, Ontario K2P 0A2

Phone: (613) 244-6090  
Fax: (613) 562-4666  
www.wfc-ottawa.ca

July 13, 2006

Board of Directors  
The Chess Federation of Canada  
E-1 2212 Gladwin Crescent  
Ottawa, Ontario  
K1B 5N1

Dear Board Members:

**Re: Management Letter on the Review Engagement of  
the April 30, 2006 Financial Statements**

During the course of our review of the financial statements of the Federation for the period ended April 30, 2006, we identified some matters which may be of interest to management. A review does not constitute an audit and consequently we do not express an audit opinion on the financial statements. We wish to emphasize that control over and responsibility for the prevention and detection of defalcations or other irregularities or errors or omissions must rest with you.

As a result of our observations on this year's review, we have outlined below some suggestions for your consideration. This letter is not exhaustive, and deals with the more important matters that came to our attention during the review. Minor matters were discussed with your staff.

- 1) The bookkeeper, Karin Bond, corrected the accounting records and verified the bank, checked inventory, payroll, etc. There was additional work on account of staff turnover and due to implementation of a new Quick Books accounting system. This arrangement for an independent bookkeeper is also prudent practice from an internal control perspective in that it provides for a greater segregation of duties.
- 2) One of the major assets of the Federation is inventory. Our analysis showed that a significant amount of the inventory is not selling or is slow moving. Although it is inevitable that a certain amount of inventory will eventually turn out to be unsaleable or obsolete, care should be taken to ensure that these types of losses are minimal. We recommend that you continue to implement special discounts and promotions on these slow moving items.
- 3) Accounts receivable have more than doubled over last year. Accounts that are over 90 days should be followed up to prevent them from becoming uncollectible.
- 4) The Federation is at risk with respect to its tax receipting procedures - this could lead to penalties and loss of tax receipting privileges. Canada Revenue Agency (CRA) has implemented intermediate penalties simply for improper receipting. Besides the risk to the Federation, failure to comply with CRA's requirements could expose directors to personal liability and expose donors to the risk that their donation receipt credits could be disallowed.

Note that CRA initiated an audit on the Chess Federation a little over a year ago. Although CRA does not appear to have followed up on their audit we understand that they advised management at that time that the Federation was not in compliance with the rules for donation tax receipts. Our own recent review indicated that the rules for tax receipting are indeed not being adhered to.

The following are CRA's general requirements with respect to which a donation tax credit can be issued:

- a) The volunteer has incurred the expenditures on behalf of the Federation.
- b) The volunteer has the right to be reimbursed for such expenditures by the Federation under an agreement between the volunteer and the Federation (i.e. the volunteer's activity and expenses are eligible for reimbursement because they are in accordance with Federation policy and programs; there is no personal benefit per se to the volunteer).
- c) The federation issues the volunteer a cheque for the amount of the expenses claimed by the volunteer and which are supported by receipts (such as airline tickets, hotel bills, etc.).
- d) The volunteer freely chooses to give some or all of the reimbursement monies back to the Federation (i.e. there can be no agreement or understanding, written or oral, that the volunteer will return the reimbursement to the Federation).

Note that it is important that there be two separate transactions – the reimbursement payment to the volunteer and the donation by the volunteer to the Federation.

We recommend that Chess Federation personnel become more familiar with tax receipting procedures as outlined in CRA's Charity Newsletters and Charity Division publications. Volunteers should be educated as to the proper requirements.

5) The Federation has incurred significant losses over the past two years and will encounter cash flow problems this year if trends continue. The solution is to increase membership revenues and to improve product sales. The other option is to take steps to significantly decrease general and administrative expenses, including salaries.

6) The following is some commentary on the financial statements:

a) The net loss from operations worsened by \$11,594, from net expenditure of \$16,277 in 2005 to net expenditure of \$27,871 in 2006. This was primarily due to an impairment in membership fees of \$7,559 and an impairment in gross profit on product sales of \$6,605.

b) Sales of books and equipment are down from \$222,878 in 2003 to \$186,769 in 2004 to \$145,398 in 2005, to \$141,883 in 2006. This decrease is due a variety of factors, including increased competition from suppliers selling chess publications and other products via the internet and also due to competition from chess retail stores. The impairment in gross profit over 2005 was mainly due to an additional write off of obsolete inventory of \$3,400 and some shrinkage in the inventory (\$2,177)

c) Looking at the balance sheet, cash decreased by \$50,690, from \$75,705 to \$25,015. This was mainly due to an operational loss of \$28K, increase in accounts receivable of almost \$12K, and a reduction in current liabilities of \$15.6K.

d) Membership fee revenues decreased by \$7,559. This was due to a drop in numbers of members from 2,676 in 2005 to 2,228 in 2006.

e) Donations (excluding donations used for the Chess Olympics and WYCC programs) decreased from \$20,545 in 2005 to \$12,807 in 2006. These basically help to finance the cost of other competitions.

f) Salaries, benefits and staff travel increased from \$50,172 to \$62,159. However this was mostly offset by a reduction in office expense from \$42,171 to \$32,674 as personnel providing "casual" (part-time) labour and professional services went onto salary.

g) Expenditures on programs increased significantly, from \$210,179 to \$233,277, an increase of \$22,092. This was primarily due to the costs of the World Youth Chess Championships and the Olympics.

h) Other programs revenue of \$165,659 (re: the Chess Olympics, CYCC, Pugi Fund and the Patron program) are offset by corresponding expenses for the same amount. The increase of \$44,356 over the prior year is primarily due to activity related to the Chess Olympics and the CYCC programs.

We have reviewed all of the issues and information in this report with Chris Mallon and Peter Arseneau and received their comments thereon. We would also like to express our appreciation for the co-operation which we received during the course of our review from Chris, Peter and Karin Bond. We shall be pleased to discuss with you further any matters mentioned in this report at your convenience.

This communication is prepared solely for the information of management and is not intended for any other purpose. We accept no responsibility to a third party who uses this communication.

Yours sincerely,

WATSON FOLKINS COREY LLP

*Brian Watson*

Brian D. Watson CA

cc: Peter Arseneau

**THE CHESS FEDERATION OF CANADA  
LA FÉDÉRATION CANADIENNE DES ÉCHECS**

UNAUDITED FINANCIAL STATEMENTS

APRIL 30, 2006

---

# Watson Folkins Corey LLP

Chartered Accountants  
70 Gloucester Street, Suite 106  
Ottawa, Ontario K2P 0A2

Phone: (613) 244-6090  
Fax: (613) 562-4666  
www.wfc-ottawa.ca

Page 1

## REVIEW ENGAGEMENT REPORT

**To the Members:**  
**The Chess Federation of Canada/**  
**La Fédération canadienne des échecs:**

We have reviewed the balance sheet of the Chess Federation of Canada/ La Fédération canadienne des échecs as at April 30, 2006 and the statements of changes in net assets and revenue and expenditure for the year then ended. Our review was made in accordance with Canadian generally accepted standards for review engagements and accordingly consisted primarily of enquiry, analytical procedures and discussion related to information supplied to us by the Federation.

A review does not constitute an audit and consequently, we do not express an audit opinion on these financial statements.

Based on our review, nothing has come to our attention that causes us to believe that these financial statements are not, in all material respects, in accordance with Canadian generally accepted accounting principles. As required by the Canada Corporations Act, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

*Watson Folkins Corey LLP*

**WATSON FOLKINS COREY LLP**  
Chartered Accountants

Ottawa, Ontario  
June 30, 2006

**THE CHESS FEDERATION OF CANADA**  
**LA FÉDÉRATION CANADIENNE DES ÉCHECS**

BALANCE SHEET  
AS AT APRIL 30, 2006  
UNAUDITED

	2006	2005
<b>CURRENT ASSETS</b>		
Cash	\$ 25,015	\$ 75,705
Accounts receivable	18,989	7,723
Inventory	67,347	70,399
Prepaid expenses	6,456	9,106
	117,807	162,933
<b>CAPITAL ASSETS (note 2)</b>	<b>92,465</b>	<b>96,498</b>
	<b>\$ 210,272</b>	<b>\$ 259,431</b>
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 14,976	\$ 17,816
Entry fees payable	8,415	17,815
Deferred membership revenue	30,017	33,406
	53,408	69,037
<b>DEFERRED CONTRIBUTIONS (note 3)</b>	<b>19,797</b>	<b>25,456</b>
<b>NET ASSETS</b>		
Invested in capital assets	91,989	96,022
Unrestricted	45,078	68,916
	137,067	164,938
	<b>\$ 210,272</b>	<b>\$ 259,431</b>

Approved on behalf of the Board:

Director

Director

**THE CHESS FEDERATION OF CANADA**  
**LA FÉDÉRATION CANADIENNE DES ÉCHECS**

STATEMENT OF CHANGES IN NET ASSETS  
 FOR THE YEAR ENDED APRIL 30, 2006  
 UNAUDITED

	2006	2005
<b>INVESTED IN CAPITAL ASSETS</b>		
Balance - beginning of year	\$ 96,022	\$ 97,137
Purchase of capital assets	-	3,874
Disposal of capital assets	-	(300)
Amortization of capital assets	(4,033)	(4,689)
Balance - end of year	\$ 91,989	\$ 96,022
<b>UNRESTRICTED</b>		
Balance - beginning of year, as previously reported	63,366	78,528
Correction of prior years' revenue (note 7)	5,550	5,550
Balance - beginning of year, as restated	68,916	84,078
Net revenue (expenditure) for the year	(27,871)	(16,277)
Purchase of capital assets	-	(3,874)
Disposal of capital assets	-	300
Amortization of capital assets	4,033	4,689
Balance - end of year	\$ 45,078	\$ 68,916

**THE CHESS FEDERATION OF CANADA**  
**LA FÉDÉRATION CANADIENNE DES ÉCHECS**

STATEMENT OF REVENUE AND EXPENDITURE  
 FOR THE YEAR ENDED APRIL 30, 2006  
 UNAUDITED

	2006	2005
<b>REVENUE</b>		
Sales of books, equipment and software	\$ 141,883	\$ 145,398
Shipping and handling charges	7,999	8,722
Membership fees	64,687	72,246
Contribution from related party (note 5)	4,806	3,963
Rating fees	24,019	27,968
Publication sales and advertising	2,348	4,530
Donations	12,807	20,545
Other programs (note 3)	165,659	121,303
Other revenue	414	248
	<u>424,622</u>	<u>404,923</u>
<b>EXPENDITURE</b>		
Cost of sales	102,611	99,521
General and administrative		
Salaries, benefits and staff travel	62,159	50,172
Building and equipment expenses	21,375	16,965
Bad debts	-	979
Office	32,674	42,171
Other executive and administration	397	207
	<u>116,605</u>	<u>110,494</u>
Programs		
Publications	49,183	48,750
International	8,975	21,467
Contributions to clubs, provincial affiliates and the Foundation	9,460	19,665
Other programs (note 3)	165,659	121,303
	<u>233,277</u>	<u>211,185</u>
	<u>452,493</u>	<u>421,200</u>
<b>NET REVENUE (EXPENDITURE) FOR THE YEAR</b>	<b>\$ (27,871)</b>	<b>\$ (16,277)</b>



# THE CHESS FEDERATION OF CANADA LA FÉDÉRATION CANADIENNE DES ÉCHECS

## NOTES TO FINANCIAL STATEMENTS APRIL 30, 2006 UNAUDITED

### 1. SIGNIFICANT ACCOUNTING POLICIES

#### (a) Organization

The Chess Federation of Canada / La Fédération canadienne des échecs was incorporated as a not-for-profit organization under the Canada Corporations Act and is a registered charity under the Income Tax Act. The Federation's mission is to promote and encourage generally in Canada, the knowledge, study and playing of the game of chess.

These financial statements do not include the accounts of the Chess Foundation of Canada as detailed in note 4.

#### (b) Inventory

Inventory is stated at the lower of cost and net realizable value. Cost is determined using the average cost basis.

#### (c) Amortization

Amortization is provided on the reducing balance basis as follows:

Building	4%
Furniture and equipment	20%
Computer equipment	33%
National library	20%

#### (d) Revenue recognition

The organization follows the deferral method of accounting for revenues. Membership fees are recorded as revenues in the period to which they relate. Restricted contributions are recognized as revenue in the year in which the related expenses are incurred. Unrestricted contributions are recognized as revenue when received or receivable only if the amount to be received can be reasonably estimated and collection is reasonably assured.

#### (e) Statement of cash flows

A statement of cash flows has not been prepared as it would not provide significant additional information.

#### (f) Estimates and Assumptions

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenditure during the reporting period. Actual results may differ from those estimates.

**THE CHESS FEDERATION OF CANADA**  
**LA FÉDÉRATION CANADIENNE DES ÉCHECS**

NOTES TO FINANCIAL STATEMENTS  
 APRIL 30, 2006  
 UNAUDITED

2. CAPITAL ASSETS

			2006		2005	
	Cost	Accumulated Amortization	Net		Net	
Land	\$ 20,000	\$ -	\$ 20,000	\$	20,000	
Building	145,502	76,690	68,812	\$	71,679	
Furniture and equipment	5,000	4,435	565		707	
Computer equipment	9,224	8,180	1,044		1,559	
National library	8,240	6,197	2,043		2,554	
	\$ 187,966	\$ 95,501	\$ 92,465	\$	96,498	

3. DEFERRED CONTRIBUTIONS

	Olympic Donations	CYCC Program	Kalev Pugi Fund	Patron Program	TOTAL
Balance - beginning of year	\$ 1,124	\$ 23,144	\$ 1,188	\$ -	\$ 25,456
Add: contributions	59,765	96,610	1,025	2,600	160,000
Less: recognized as revenue	(60,000)	(104,975)	(500)	(184)	(165,659)
Balance - end of year	\$ 889	\$ 14,779	\$ 1,713	\$ 2,416	\$ 19,797

Olympic donations are designated to provide financial support for participation of Canadian representatives in the International Chess Olympiads. The Canadian Youth Chess Championships (CYCC) entry fees and donations cover the cost of sending players to the world championships. The Kalev Pugi Fund was established as a bequest in the Chess Foundation of Canada. Each year interest earned by this Fund is transferred from the Foundation to the Federation to provide travel assistance for junior players. The Patron program was established to improve magazine production.

Contributions to these programs are recognized as revenue in the year in which the related expenditures are incurred.

4. CONTINGENT LIABILITY

Canada Revenue Agency (CRA) commenced an audit of the Federation's books and it is not yet completed. CRA is contesting the validity of certain tax receipts that have been issued for donations relating to international competitions. CRA has also indicated the possibility of additional liability relating to unremitted payroll deductions; because this amount is unknown, it has not been accrued for in the accounting records.

**THE CHESS FEDERATION OF CANADA**  
**LA FÉDÉRATION CANADIENNE DES ÉCHECS**

NOTES TO FINANCIAL STATEMENTS  
 APRIL 30, 2006  
 UNAUDITED

5. RELATED PARTY TRANSACTIONS

The Chess Foundation of Canada is effectively controlled by The Chess Federation of Canada since the Federation appoints the Foundation's Board of Trustees. The Foundation was established as a trust to financially help the Federation promote and develop chess. Donations of \$750 (2005 - nil) and life membership fees of nil (2005 - \$1,070) have been paid into the Foundation from the Federation. The Foundation has contributed \$4,806 (2005 - \$3,963) in support of the Federation's general operations and \$1,025 (2005 - \$1,025) towards the Kalev Pugi junior program.

The Foundation has not been consolidated with the Federation's financial statements. Unaudited and unconsolidated Chess Foundation of Canada financial summaries as at April 30, 2006 and 2005 and the years then ended are based on data provided by another firm of accountants, as follows:

	2006	2005
<b>BALANCE SHEET</b>		
Assets	\$ 155,149	\$ 150,154
Liabilities	-	-
<b>Net assets</b>	<b>\$ 155,149</b>	<b>\$ 150,154</b>
<b>STATEMENT OF REVENUE AND EXPENDITURE</b>		
Revenue	\$ 11,216	\$ 7,134
Expenditure	6,221	5,363
<b>Net revenue for the year</b>	<b>\$ 4,995</b>	<b>\$ 1,771</b>

6. FINANCIAL INSTRUMENTS

The carrying value of cash, accounts receivable, accounts payable and entry fees payable approximate their fair value because of the relatively short period to maturity of the instruments. Unless otherwise noted, it is management's opinion that the Federation is not exposed to significant interest, currency or credit risks.

7. CORRECTION OF PRIOR YEARS' REVENUE

The deferred membership revenue of prior years has been corrected by \$5,550.

8. COMPARATIVE FIGURES

Certain of the comparative figures have been reclassified to conform with the current year's presentation.